9/19/84

Memorandum 84-81

Subject: Comments on Commission Meeting Materials

Attached is a letter forwarding to the Commission the comments of the Executive Committee of the Probate and Trust Law Section of the Los Angeles County Bar Association with respect to various matters to be considered at the Commission's September meeting.

This memorandum is listed on the Fianl Agenda for the meeting under each item to which a comment contained in the attached letter is relevant.

Respectfully submitted,

John H. DeMoully
Executive Secretary

Los Angeles County Bar Association

Probate and Trust Law Section

617 South Olive Street
Los Angeles, California 90014
213 627-2727

Mailing address:
P.O. Box 55020
Los Angeles, California 90055

September 13, 1984

California Law Revision Commission
4000 Middlefield Road, Room D-2
Palo Alto, California 94306

Re: September Meeting

Dear Commissioners:

The Executive Committee of the Probate and Trust Law Section of the Los Angeles County Bar Association submits the following comments on various studies which are scheduled for discussion at your meeting September 27-29, 1984. First, however, we would like you to know that we appreciate the conscientious consideration given by the staff to our comments and the incorporation of our suggestions in revised proposals to the Commission.

Study F-601 Jurisdiction over Joint Tenancy and Tenancy in Common Property at Dissolution of Marriage (Memorandum 84-59).

In a marital dissolution proceeding, the Court has jurisdiction to settle the property rights of the parties but only as to community property. Property held as joint tenants or tenants in common must be divided in a separate partition action. To cure this problem, it is recommended that the Court be given jurisdiction to divide separate property at the request of either party. This would add economy and flexibility to the proceedings it is believed.

While this particular memorandum is outside the usual area of law on which we make comments, we have reviewed the case of In Re Marriage of Leversee and concur with the conclusions of the Court of Appeal. Since the tax objections to such legislation have been removed by action of Congress, we believe it would be appropriate to add such legislation at this time.

Our general agreement with the staff recommendation includes some questions and observations. What protection is there for the rights of third parties who are tenants in common or joint tenants with the marital partners? The proposed addition of new Civil Code §4800.4 specifies, inter alia, that noncommunity property would be divided with the same procedure and subject to the same limitations on division of community property or quasi community property. We suggest that careful consideration be given to the powers and discretion given a court under Civil Code §4800 which exceed the valuation and equal division of community assets. Is it appropriate that a Court have these same powers and discretion over noncommunity property assets?

Study F-521 Community Property in Joint Tenancy Form (Memorandum 84-69).

As noted in our letter of June 9, 1984, we have reservations as to whether the study recommendations should be enacted into law. The concepts of community property and joint tenancy are well established in the law. These classifications of title have been a useful part of our society for many years. Any difficulty with form of title stems from the failure of those taking title adequately to understand the difference of one from the other or to obtain adequate counseling. The recommendations seek to remedy a problem perceived by the staff by altering the definition of forms of title. It is submitted that this is unnecessary and will likely do more harm than good.

It is commonly acknowledged that before the 1970's a very high proportion of family assets were held in joint tenancy between husband and wife although community funds were used to make the purchase. The reasons for this vary, but in large part it was common practice for real estate brokers to tell buyers that this was how everyone did it when buying a house and it was well known that holding title as joint tenants would avoid probate.

Today, rampant inflation in the housing market has pushed land values to unimagined heights. In reading over the staff recommendation, it is clear that the moving force for change is a need to address the common law concept of community property in joint tenancy form which has grown over the years and which, in large part, is relied upon by lawyers to gain for their clients a step-up in basis on both halves of property on the death of a spouse and thereby gain future income tax advantages.

We believe that the problem which is perceived by the staff will resolve itself over time due to changes which commenced approximately a decade ago. The revision in the Probate Code in the early 1970's makes the transfer of title to community property on death just as easy whether held in joint tenancy form or as community property. With time, it is anticipated that holding title as community property will become much more common. It has also been our experience that reputable real estate brokers now refrain from advising prospective buyers as to how title should be held and direct buyers to seek counseling from their attorney. As taking title in joint tenancy is replaced by community property, a form of title which avoids probate, truly reflects the ownership interest of the parties, and is more useful to the property owner (e.g., step-up in basis on death) the problem should resolve itself.

The alternative proposed by the staff of the Law Revision Commission would create the anomaly of joint tenancy which is not joint tenancy. Community property held by husband and wife in joint tenancy would be community property at death unless a third party became a joint tenant which would mean that the property would be owned in joint tenancy. But again, if the third party died then the property would presumably no longer be joint tenancy but community property on the death of one of the spouses unless there was a more specific writing stating that the husband and wife really meant it when they put title to the asset in joint tenancy. Lou Costello, if asked about all this, might very well ask, "Who's on first?" The proposed solution creates too many new rules and traps for the unwary.

The proposal makes it unnecessarily difficult for persons to hold property in true joint tenancy. It would no longer be sufficient simply to use commonly understood language, but rather, additional statements would be required on the title document or a separate agreement between husband and wife would be needed. This would presumably require the time and expense of an attorney. As a practical matter, there are some documents, such as stock certificates, where it may be difficult to convince a transfer agent to add the requisite language to establish that a true joint tenancy relationship is intended.

Further, the recommendation, we believe, is unduly harsh in that no tracing is permitted to establish the separate source of a particular asset, nor is a person who makes a contribution from separate property entitled to receive anything more than reimbursement of that which was contributed to the purchase. The proposal allows no participation in the appreciation of the value of the asset.

The use and effect of joint tenancy is generally known in California by the public. The proposed changes would certainly alter this with attendant confusion until the new law is learned. In addition, such a proposal would alter many estate plans as joint tenancy property would be subject to testamentary disposition. A man may now pass assets on death to his wife by having her as a joint tenant with right of survivorship on such assets. The residue of his estate could be left by Will to children or others. This same Will under the recommendations could cause all assets to pass to residual distributees under a Will, and leave the widow with only her share of community property.

As a final point, what effect, if any, would the recommendations have on quasi-community property held in joint tenancy?

Study L-605 Probate Law and Procedure (Distribution under a Will or Trust) (Memorandum 84-65 and First Supplement).

We are in agreement with the staff proposal for modification of Probate Code Sections 240, 250, 251 and 252

regarding definitions of per stirpes and per capita under Wills, Trusts and intestate succession. Further, we agree that the proposed amendment to Section 251 be made retroactive.

Study L-658 Distribution of Small Estates without Administration (Memorandum 84-66 and Supplement).

The Law Revision Commission proposal deals with the fact that, under current law, probate administration is required if a decedent dies owning real property which does not pass to a surviving spouse, regardless of the value of the property. Under the proposal, a summary proceeding is established to deal with the situation, when the combined value of real and personal property falls within the limits of Probate Code Section 630 ($60,000). The summary proceeding is patterned after the community property "set aside" procedure (Section 650-657). The proposal also eliminates the present requirement of Probate Code Section 630 that the value of the decedent's real estate in California must be below $10,000. Under the revised version of Section 630, if a decedent's estate is below $60,000, personal property can be collected by Affidavit and real property can be confirmed by Court Order.

We recommend that the Commission adopt the proposal. Although experience has taught that the community property confirmation proceeding is not dramatically easier than a probate, it does eliminate some of the steps, and the proposal would have the same effect for small estates involving real property.

The proposal would allow the transfer of title to a vessel by Affidavit without any limitation as to value. We do not see any reason why vessels should not be subject to the $60,000 limitation applicable to other kinds of property. It has often been facetiously said that a boat is nothing more than a hole in the water into which money is poured. Certainly, a large number of vessels are of such significant value that the administrative safeguards of probate administration should apply.

Study L-640 Trusts - Trustee's Powers (Memorandum 84-22).

Section 4472 (Loans to Beneficiary): We agree with the proposed change with regard to loans from trust assets.

Section 4478 (Hiring Persons): We agreed that the trustee should be able to retain accountants. However, we are still troubled by the question of delegation of discretion. We are reluctant to authorize the trustee, who was selected presumably because the trustor trusted his judgment, to permit another person to make decisions which the trustor assumed the trustee would make. Further, while the staff may not find the "administrative v. discretionary" distinction as clear as we do, we have trouble with the staff's proposed use of a prudent man rule. Such a rule has caused enough problems in the investment area where it has long been used, and we do not see any advantage in attempting to insert it into the area of delegation of powers and duties. We suspect that such a standard will result in even less delegation than presently occurs since an individual is likely to perform many acts himself which a corporate trustee would delegate.

Section 4402 (Conflict of Interest in Exercise of Power): We believe that there may be some merit in codification of a standard based on the Pitzer decision and that further review and consideration is warranted.

Breach of Trust (Memorandum 84-23 and First Supplement).

Measure of Damages: We support the adoption of Restatement Sections 204 and 205, and we agree that the "good faith exception" contained in Comment g to Section 205 should be included in the statute itself, rather than in the Comments.

Interest: On review of the First Supplement and the comments to Restatement Section 207, we agree with the staff recommendation so long as the Restatement Comments are included with the comments to proposed legislation.

Co-Trustee Liability: We are still concerned about the extent to which a co-trustee is required to "redress" a breach of trust, for the reasons discussed in our June 8, 1984 comments. The balance of Restatement Section 224 is acceptable.

Limitations: We would be willing to accept the statute of limitations as proposed, as long as it is clear that it will not be available in instances where a court order was obtained. We would request a change in the reference to "the person's representative" in subsection (b). This term is not defined, and we wonder if it is limited to the legally-appointed representative of the minor or disabled person. In that case, it would be necessary to have the court appoint a guardian for a minor just so that there would be someone to whom accountings could be sent. If it is not so limited, a wide variety of people could fall into the category of "representative". The trustee is entitled to know with some degree of certainty to whom the accounting should be sent. We suggest that the staff consider language such as "the parent or legal representative of the person".

Exculpation: As indicated in our June 8, 1984 comments, we disagree with the staff's interpretation of Probate Code Section 2258. That statute states that the trustee shall have "no liability to any person". It would certainly seem to relieve the trustee of all liability to the beneficiaries for following the trustor's directions, but the staff states that the trustee "cannot operate free from all liability" to the beneficiaries. What liability, then, does the trustee have if he followed the instructions of the trustor? Does the trustee have an obligation to refuse to follow the trustor's instructions if he feels that they are not in the best interests of all of the beneficiaries? The trustor may have intended to treat some better than others. At what point is the trustee to start second-guessing the trustor? It is correct that Restatement Section 222 does not hold the trustee harmless against all liabilities but the only ones described in that section against which the trustee will not be held harmless are those involving bad faith breaches of trust or abuse of a confidential

relationship with the trustor. What other types of liability does the staff believe to be excluded from Section 2258?

Liability of Trust and Trustee to Nonbeneficiaries (Memorandum 84-24 and Supplement).

We agree with the staff that the trustee should not be protected from negligent conduct and therefore we do not agree with the suggestion of the CBA that they should be. Our reason for preferring the language of the Restatement Second of Trusts Sections 265 and 264 is that we believe that they are better worded and clearer than Sections 4521 and 4522.

While we agree with the staff that the revisions suggested by the CBA with regard to the duty now owed to third persons is overly broad, we have heard of many situations where creditors of a beneficiary have sued the trustee because the trustee has failed to agree to exercise a discretion in favor of invasion of principal in a way which might benefit the creditor. It may not be a bad idea to codify Restatement Section 200 in order to avoid these sorts of suits which are an expense to trustees and trusts, even if they are eventually successful against the person who is not the beneficiary.

We believe that Section 4544 should be continued and that the amendment suggested by the CBA is desirable.

We would have no problem with the staff's suggestion that the trustee be expressly permitted to retain property and withhold payments in lieu of imposing a "trustee's lien." (Section 4531).

We reiterate our belief that a power to revoke should be treated in the same manner as a general power of appointment, as far as the rights of credits are concerned, for the reasons discussed in our June 8, 1984 comments. We would support the proposed optional four-month creditor's claim period, described in the letter from Estelle Depper.

As stated in our June 8, 1984 comments, we do not believe that revocable trusts should be subject to the same formalities as wills.

Office of Trustee (Memorandum 84-26).

Section 4500 (Trustee's Compensation): Some courts, upon petition, will order periodic payments of compensation to the trustee, to continue for an indefinite period of time, in order to avoid the necessity of annual petitions for fees. Other courts, however, have been reluctant to do so. Perhaps making it clear that the Court does have this power would help to eliminate routine fee petitions. We have no objection to permitting the beneficiaries to agree to higher compensation than that previously approved by the Court. If the beneficiaries have approved the compensation, it should not be necessary to use court time to have that approval confirmed by the court.

Section 4551 (Trustee's Bond): We have no objection to exempting corporate fiduciaries from the bond requirement in view of the reserve requirements. We are aware of no instance in which the lack of a bond by a corporate trustee has resulted in any damage to a beneficiary.

Section 4560 (Actions by Co-Trustees): We would accept the change from unanimity to majority rule if the dissenting trustee is relieved of liability for the actions of the majority. We would be concerned about majority rule if the dissenting trustee is to be held liable for the acts of the majority even though he opposed such actions. If Restatement Section 224(2)(e), discussed in Memorandum 84-23, is to be codified, the dissenting trustee will be liable for failing to redress a breach of trust committed by his co-trustees. It is thus up to the dissenter to decide at his peril whether an action proposed by his colleagues is simply unwise or constitutes a breach of trust. The very fact that he did dissent will be used to prove that he knew that the proposed action was improper.

Section 4561 (Inability of Co-Trustee to Act): We would accept the changes proposed by the CBA, and we agree that the phrase "legally incapable of acting" is too restrictive. "Legally incapable" may require that a conservator have been appointed or some legal determination of incapacity have been made. A physically incapable or mentally incapable co-trustee may still be legally capable to serve.

Section 4570 (Resignation of Trustee): We agree that a majority of the beneficiaries should be able to accept the resignation of the trustee. To require unanimity would permit one beneficiary to force the trustee to go to court to tender his resignation, resulting in unnecessary expense.

Section 4572 (Removal of Trustee): We agree completely that creditors should not be permitted to interfere in the administration of a trust. The right to remove the trustee should belong to the beneficiaries of the trust.

Section 4573 (Vacancy in Office of Trustee): We agree that the resigning trustee should continue to administer the trust until the assets are distributed to the successor trustee.

Section 4580 (Appointment of New Trustee): We see no problem with permitting the court to appoint a greater number of trustees than were appointed by the trustor, unless the trust instrument specifically limits the number of trustees, and we agree that creditors should not have the right to petition for the appointment of a new trustee.

Judicial Administration (Memorandum 84-29 and First Supplement).

Please refer to our comments as set out in our letter of June 8, 1984.

Transfer of Trusts to and from California (Memorandum 84-30 and First Supplement).

This Memorandum deals with the proposed revision of the statutory provisions for transfer of the administration of testamentary and inter-vivos trusts from another jurisdiction to California and also transfers from California to another jurisdiction. The Commission changes were brought about not as a result of any serious problem with the current statutory provisions (Probate Code Sections 1139-1139.19) but as a part of the overall revision and relocation of all of the statutory provisions regarding trusts. In addition to renumbering the sections, the proposal clarifies certain aspects and attempts to eliminate superseded or redundant provisions. We are in agreement with the staff proposal.

Revised Uniform Principal and Income Act (Memorandum 84-32 and First Supplement).

Please see our comments in our letters dated April 16 and June 8, 1984.

We believe that draft Section 4815 should remain unchanged. At the same time, we disagree with the suggestions made by CBA in their June 18, 1984 comments to this section. We find it difficult to imagine a situation where a trustee, exercising reasonable discretion and acting with regard to duties to both income beneficiaries and remaindermen, would not be compelled by his duties to create a reasonable reserve for depreciation or depletion. The determination of a reasonable useful life, of course, need not correlate with the useful lives established for tax purposes. The only situation where no reserve may be required is where the trust has manifested an overriding intent to benefit the income beneficiary in all circumstances and has stated that the rights of remaindermen are negligible. In those unusual situations, a rule requiring depreciation or amortization could be avoided by the drafter of the document.

Presumption of Revocability as to Foreign Trusts (Memorandum 84-34 and First Supplement).

We agree with the staff recommendation that comments to draft Section 4201 clarify that "resident" is synonymous with "domiciliary" by citing Estate of Glassford.

When the intention of the trustor is contained in the instrument, we believe that intention should be controlling. When it is not contained in the trust instrument, however, we believe that the intention of the trustor as to the law governing the construction of the trust should not be limited to the trust instrument, but should be determined upon the circumstances of the creation of the trust and the usual factors that would be used for such determination. Correspondence between the trustor and the attorney, statements made by either at the time of preparation of the document, etc., could obviously be relevant. We generally concur with the staff suggestion.

Oral Trusts (Memorandum 84-25 and First and Second Supplements).

We believe that oral trusts should be abolished. Some writing should be required in order to create an express trust. Continued reliance on oral express trusts is an invitation to litigation and to perjured testimony. The law of constructive and resulting trusts is adequate to protect most individuals who would otherwise be affected by oral trusts. The inability to determine with certainty the terms of oral trusts, even if the beneficiaries are clearly understood and identified, creates more problems than is desirable. We concur with the analysis of staff counsel Stan Ulrich in the Second Supplement.

Conduct of Trust Business and Qualification by Foreign Trustees (Memorandum 84-27).

As we mentioned in our April 16, 1984 comments, we see a number of advantages to limited reciprocity. In particular, it would be helpful if California corporate

fiduciaries could serve as fiduciaries in connection with real property located in other states. However, before taking any definite position, we would certainly be interested in the comments of the CBA.

Validity of Trusts for Indefinite Beneficiaries or Purposes (Memoranda 84-19 and 84-31, and First Supplement to Memorandum 84-31).

We agree with the Commission's proposals for the reasons stated in our April 16, 1984 comments.

Study L-654 Ancestral Property Doctrine (Memorandum 84-70).

This Memorandum deals with the question of whether Probate Code Section 6402.5 (the successor to Section 229) should be retained. This Code Section deals with the situation where the decedent dies intestate, is not survived by spouse or issue and owns property which can be traced to a predeceased spouse (either as the predeceased spouse's half of the community property or separate property of that spouse). The present statute provides that real property received from a predeceased spouse within 15 years prior to the death of the present decedent passes to the heirs of the predeceased spouse.

The Study states numerous reasons against the ancestral property doctrine and recommends its abolition and repeal of Section 6402.5. We are in agreement.

Sincerely,

EXECUTIVE COMMITTEE, PROBATE
AND TRUST LAW SECTION

By Richard L. Stack
Richard L. Stack

RLS:lgc