

First Supplement to Memorandum 85-65

Subject: Study L-800 - Probate Code (Abatement; Distribution of Interest and Income)

Attached to this Supplement as Exhibit 1 is a letter from Irving Goldring, one of the designated State Bar advisors who reviewed the basic Memorandum and draft statute. Mr. Goldring's letter concerns the draft statute attached to the basic Memorandum. His comments are discussed below.

Pro Rata or Hierarchical Abatement?

Under existing California law, if the estate is insufficient to satisfy all of the testator's general and specific devises, they are reduced (abated) in proportion to their respective values. Prob. Code § 750. The draft statute attached to the basic Memo abandons the pro rata rule in favor of a hierarchical rule of abatement: All general devises must first be exhausted before any reduction is made in specific devises. See proposed Section 6183. The hierarchical rule is consistent with the Uniform Probate Code and the rule generally applicable elsewhere in the United States. Professor Halbach is not sure that the proposed change is an improvement, and the staff has some misgivings. Mr. Goldring does not like the proposed change, and thinks that the existing pro rata rule is more consistent with the intent of most testators.

Mr. Goldring correctly points out that the proposed hierarchical rule is inconsistent with the existing pro rata abatement rule when the share of a spouse or child omitted from the testator's will is paid. See Prob. Code §§ 6562, 6573. However, the Commission approved those two sections with the intent to preserve existing law, with the understanding that the question would be reexamined when Section 750 was revised. We are now at that point. If the Commission decides to adopt a hierarchical rule of abatement, Sections 6562 and 6573 will, of course, have to be conformed.

The proposed change is less extreme than might appear at first, because the court has broad discretion under the proposed rule as well as under existing law to deviate from the statutory abatement rule to carry out the testator's intent. See Prob. Code § 750; proposed Section 6183. Nonetheless, the choice between the pro rata and hierarchical abatement rules is the central policy issue presented by the draft statute.

Interest on Unpaid Devises

The draft statute codifies case law by providing that interest is simple interest unless there has been a willful breach of duty by the personal representative, in which case interest is compound. See proposed Section 6184. Mr. Goldring thinks the provision for compound interest should be located with general provisions governing breach of duty by a personal representative. The staff will flag this provision for possible relocation when the general provisions are completed.

Existing law provides that overdue periodic payments or trust income draw interest, computed on the unpaid accumulations held by the personal representative "on each anniversary of the decedent's death." The draft statute revises this to provide that interest is computed on unpaid accumulations held by the personal representative "after the payment date." Proposed Section 6187(c). This revision provides for a computation of interest which is more mathematically exact, but is somewhat more complex. Mr. Goldring would keep the simpler formulation of existing law. The staff has no strong view. Does the Commission wish to restore existing law?

Drafting Suggestions

Proposed Section 6180 generally continues definitions found in existing Section 662. Mr. Goldring has a problem with some new words found in proposed Section 6180, but not in existing law. The proposed definition of "annuity" describes it as a "general or demonstrative" devise. The proposed definition of "demonstrative devise" describes it as a "general" devise. This is necessary to make clear that the abatement rules for general devises in proposed Section 6183 apply to annuities and demonstrative devises, and that the interest rules for general devises in proposed Section 6186 apply to demonstrative devises. The same result could be accomplished by deleting those

words from the definitions, by revising Section 6183 to refer to "[g]eneral devises, including annuities and demonstrative devises," and by revising Section 6186 to refer to a "general pecuniary devise, including a demonstrative devise." Would this be an improvement?

The staff agrees with Mr. Goldring's suggestion to substitute the word "satisfied" for the word "made" at the end of subdivision (d) of Section 6180, and will make that change.

The staff does not agree with Mr. Goldring's suggestion to revise the title of the article to read: "Devises, Abatement, Interest, and Income." The article does not apply to devises generally, but only to abatement of devises, and to interest and income on devises. To revise the title as suggested would imply that the article applies to devises generally, and would thus be misleading.

Respectfully submitted,

Robert J. Murphy III
Staff Counsel

EXHIBIT 1

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June 17, 1985

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4000 Middlefield Road, Suite D-2
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Re: Memorandum 85-65
L 800 June 3, 1985

Dear Mr. Murphy:

Mr. Rae advises me that we (particularly I) have tarried over earning a living too long, and that you have moved forward with Memorandum 85-65 without our response to your letter of April 11, 1985. None-the-less, I am writing on our behalf with comments in the hope they may influence a First Supplement to Memorandum 85-65.

I will respond to one of your general comments first and then move on to more specifics.

1. In the second paragraph of your letter you responded to our concern about redrafting Division III rather than merely improving it, particularly as it may imply a change in substance. You indicated the drafting of the Probate Code was an "atrocious mess". That may be, but it is now an interpreted "atrocious mess". Statutes are seldom perfect but are the basis for the conduct and control of specific areas of the law the interpretation of which have been left to our courts. The combination of statutes and cases gives us a body of law and some certainty in it. A redrafted, substantively changed statute will give attorneys and courts another 18,000 cases to develop. Unless there is good reason to abandon the established body of law there is no reason for substantive change. Many of the comments indicated a change of substance.

I had believed the work on Division III was to be "clean up", not change. Moving from what we have to statutes based on the UPC are substantive.

2. For a second time I suggest the article title should begin with "Devises" since the article starts off defining devises and is the only place those definitions appear. This would give those seeking such information two places to look: the table of contents and the index.

3. §6180(a): The words "general or demonstrative" which are not present in current §662(b) should be deleted.

4. §6180(b): Perhaps I am a little dense but I am not quite sure why a "demonstrative devise" is a "general devise". Present §662(e) says "all other legacies are general legacies" and §662(b) defines "demonstrative" legacies without saying they are "general legacies". Therefore, how are "demonstrative" devises "general" other than by changing the definition in proposed Section 6180(b) by adding the word "general" to the definition of demonstrative? Is this a substantive change?

5. §6180(d): Mr. Rae feels the last word of the sub-section, "made" is inappropriate and should be left as it is, "discharged, or perhaps be changed to "paid". I vote with him to keep "discharged" or use "paid" or use "satisfied", but not "made".

6. §6183: We still believe that abatement and priority for payment are separate concepts and that their combination in this Section creates a major conceptual problem. This problem is exacerbated by the addition to this draft of "satisfying a share of a spouse or child not provided for in the testator's will." The result is a direct conflict with the provisions of §§ 6562 and 6573, which satisfy such share first out of undisposed of property (which is consistent with this Section) and then proportionately from all devises (which is inconsistent with this Section). As to (b)(2), we preferred the prior draft which first abated Residuary devises to unrelated persons, and then abated Residuary devises to spouse or kindred. That formula was consistent with the balance of the sub-section. We disagree with the deletion of (e) from the former draft re failure of a specific devise. We disagree with the pink sheet comment on repealed § 662 that it's covered by other Sections.

In regard to the discussion concerning the abatement of general and specific devises, we think there is some confusion and the provisions of § 750 are better than those provided in proposed § 6183. Very often a testator is much more interested in the recipient of a general or demonstrative devise than a specific devise: the specific devise may be an item of small value and by definition is an item which the testator has no intention of replacing for that devisee in the event it does not exist at the testator's death, and very often a demonstrative gift of money is an equalizer for

Robert J. Murphy III, Esq.
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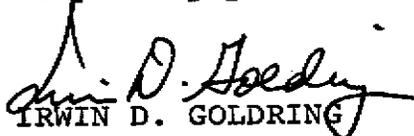
a specific devise and, therefore, if not prorated the result would be in opposition to the intent of the testator.

As to sub-section (d) in regard to the proposal to give the Court discretion whether to abate to favor spouse and kindred, this simply creates new ground for litigation, contrary to the prevailing effort of the Code reforms to reduce the burden in the Court. The mechanical rule is based on sound public policy and should not be discarded.

7. § 6184: Why is there a sub-section(b)? The rate of interest which is being discussed in these sections is merely defining a rate in terms of amount and has nothing to do with penalty. Subsection (b) is completely out of place. This type of wording and thinking belongs in a section dealing with the penalties applicable to breach of duty by a fiduciary.

8. § 6187(c): How is interest to be computed? On what balance? Determined annually, as under present law, or quarterly, monthly, or what? The Memorandum at the top of page 5 misconstrues § 663(c). It does not provide for compound interest, it states a simple formula for how to compute interest--"on the amount of...accumulations...held... on each anniversary of the decedent's death, computed from the date of such anniversary." We would retain the present simple formula.

Very truly yours,


IRWIN D. GOLDRING

IDG:hs

cc: Matthew S. Rae, Jr., Esq.
Charles A. Collier, Jr., Esq.
Kenneth M. Klug, Esq.