First Supplement to Memorandum 88-45

Subject: Study L-3010 - Fees of Corporate Trustees (California Bankers Association Revised Draft Statute)

Attached to this supplement is a revised version of the California Bankers Association draft statute relating to corporate trustees' fees and replacement of trustees. (See letter from David W. Lauer, Chairman, California Bankers Association Trust State Governmental Affairs Committee, in Exhibit 1.) This draft supersedes the earlier draft in Exhibit 2 to Memorandum 88-45.

In addition to a number of technical revisions, this draft differs in several important respects from the earlier draft:

(1) The description of fee increases covered by the statute has been expanded to cover base fees and minimum fees, in addition to percentage fees.

(2) Where the trustee and the beneficiaries are unable to agree, the draft provides a formal procedure permitting all beneficiaries to select a replacement trustee within 60 days following the stated effective date of the proposed fee increase. Selection of the successor trustee may be accomplished without court approval by a method provided in the trust or otherwise by agreement of all beneficiaries (as defined). Selection of a successor may also be accomplished by all beneficiaries with court confirmation or on petition of an interested person, where all beneficiaries cannot agree.

(3) The revised CBA draft also includes a provision that would limit the liability for exemplary damages to three times the amount of compensatory damages. (See Section 16443 on the last page of Exhibit 1.)

The exemplary damages provision has an interesting background. It is essentially the same as a section proposed by the Commission in the Trust Law. However, this provision was opposed by the California Trial Lawyers Association when the bill proposing the Trust Law was heard by the Assembly Committee on Judiciary and there were not enough votes to get the bill out of committee in light of the opposition. Accordingly, the exemplary damages provision was eliminated. Following enactment of the Trust Law, the Commission had before it a proposal to put the exemplary damages provision in a separate bill. When we first considered the question of corporate trustees' fees and replacement of trustees, it was suggested that these matters be combined into one bill. When the State Bar and CBA agreed to work on a bill relating to trustees' fees for Assemblyman Harris, without Commission involvement, the Commission was left only with the exemplary damages part of the bill.

Meanwhile, Senate Bill 241 -- the Willie L. Brown Jr.-Bill Lockyer Civil Liability Reform Act of 1987 -- was enacted. (See 1987 Cal. Stat. ch. 1498.) This legislation relates to contingency fees in actions against health care providers, to product liability exemptions, to relations between insurers and insureds in litigation, to the punitive damages for breach of contract, and to related matters. Senate Bill 241 does not specifically cover punitive damages against trustees or otherwise arising in fiduciary relationships, although it did amend Civil Code Section 3294 governing punitive damages in actions for breach of obligations not arising from contract. In November of last year, the staff contacted the Senate Judiciary staff to investigate the prospects of a bill limiting exemplary damages against trustees. We were told that it would be futile, that such a bill would not pass, and that Senate Bill 241 speaks exclusively on this subject for the time being. Accordingly, we have not pursued the earlier proposal.

Now it is again before us in the CBA draft. The Commission may want to test the waters in 1989 and see whether the assessment of the chances of such a bill given in November 1987 are accurate. The staff would not include such a provision, but if it is in the bill and engenders significant opposition, it can be dropped as it was from the trust bill in 1986.

Respectfully submitted,

Stan G. Ulrich
Staff Counsel

California Bankers Association

Established 1891

June 22, 1988

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
Suite D-2
4000 Middlefield Road
Palo Alto, California 94303-4739

Re: Trustees Fees (Memoranda 88-36 and 88-45)

Dear Mr. DeMoully:

The California Bankers Association appreciated the opportunity offered by the California Law Revision Commission to appear before the Commission on May 6, 1988 for the purpose of presenting the CBA's views on the subject of trustee fees.

Based on the discussion at the May 6 meeting, the CBA has reviewed and revised its original proposal as presented in my letter to you of March 7, 1988. I am enclosing a copy of the revision dated June 22, 1988 with this letter.

The revision contains several changes to the original proposal. The most significant change is the addition of a right for beneficiaries to substitute trustees without court intervention under defined circumstances.

The CBA continues to believe that there is no problem which requires a legislative solution. As reflected by the statements of the CBA members at the May 6 meeting, existing law and practices of trustees provide significant remedies for beneficiaries. Nevertheless, as previously stated to you, in the spirit of further promoting the interests of trust beneficiaries, the CBA has drafted this revised proposal.

I would like to discuss the CBA proposal with you prior to the Commission meeting of July 14-15, 1988. To this end, I will contact you during the week of June 27 to arrange a mutually convenient time and place.

For your information, I am providing a copy of this proposal to the State Bar Estate Planning, Trust and Probate Law Section for their consideration.

We welcome the opportunity to work with you further on this subject.

Sincerely yours,

David W. Lauer

David W. Lauer
Chairman, California Bankers
Association Trust
State Governmental Affairs Committee
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DWL:dp

Enclosure

Draft 6/22/88

OVERVIEW OF PROPOSED LEGISLATION

RECOMMENDED BY CALIFORNIA BANKERS ASSOCIATION

This proposal adds the following provisions to the existing Trust Law.

1. Mandates a policy under which a trustee must give beneficiaries (as defined) 60 day advance written notice of a proposed increase in compensation before the increase in the rate of compensation is implemented. The notice provides beneficiaries with information important to their interests. In addition, the proposal confers on beneficiaries rights not currently provided to them under existing law.

2. Provides that all beneficiaries (as defined), may, within a specified time frame, change trustees if the trustee increases its compensation.

3. Provides a limitation on punitive damages against trustees.

Existing: Increase in Compensation

15681(a) existing

15681(b) The trustee may increase its stated periodic (1) base fee, (2) rates of percentage compensation, or (3) minimum fee (hereinafter collectively referred to as "compensation") only after compliance with the requirements of this Section.

(1) The trustee shall provide written notice in the manner specified in this Section at least sixty days prior to the stated effective date of the increase in compensation to all beneficiaries, as defined in Section 15681(b)(5), for those trusts affected by the increase.

(2) The notice shall contain the following information:

(i) The effective date of the increase.

(ii) The current and the proposed compensation.

(iii) The name, address and telephone number of the person or persons representing the trustee to whom questions may be addressed.

(iv) A statement that, if all the beneficiaries object to the increase in a writing delivered to the serving trustee, the serving trustee has until the thirtieth day following the stated effective date of the increase, to determine to withdraw or compromise the increase. During such 30 day period, no increase shall be implemented.

(v) A statement that if all the beneficiaries object to the increase in a writing delivered to the serving trustee and if the serving trustee does not withdraw or compromise the increase, subject to any contrary provision of the trust, all the beneficiaries may, prior to the sixtieth day following the stated effective date of the increase, (1) select a new corporate trustee, or (2) select a new individual trustee subject to confirmation of the court.

(3) If prior to the stated effective date of the increase, all of the beneficiaries, as defined by Section 15681(b)(5), object to the increase in a writing delivered to the trustee, the serving trustee may in writing withdraw or compromise the proposed increase to compensation at any time until the thirtieth day

following the stated effective date of the increase. During such 30 day period, no increase shall be implemented.

(4) If, prior to the stated effective date of the increase, all of the beneficiaries, as defined in Section 15681(b)(5), have objected in writing to the increase, and the increase has not been compromised or withdrawn pursuant to section (3), all the beneficiaries may, prior to the sixtieth day following the stated effective date of the increase, select a successor trustee pursuant to Section 15661. During such 60 day period, no increase shall be implemented. A trustee who is removed pursuant to this section shall not be liable to any person for any consequences of the substitution, and shall not be liable for the selection, acts or omissions of a successor trustee.

(5) For purposes of this Section, the term "all beneficiaries" means: (1) the person, if any, holding the power to revoke the trust; or if none, (2) the present holder of a general power of appointment over, or power to withdraw, all property from the trust, or if none, (3) all beneficiaries to whom income or principal is required or authorized in the trustee's discretion to be currently distributed, or who would

be entitled to receive a distribution of principal if the trust were terminated at the time notice is given, subject to the limitations in Section 15800.

If any such beneficiary is a ward or conservatee, the notice required by Section 15681(b)(1) shall be sent to the guardian or conservator, as the case may be, of the beneficiary. If such beneficiary is a minor for whom no guardian has been appointed, notice shall be sent to the parent having legal custody of the minor. The guardian, conservator or parent of such a beneficiary shall represent the interests of the beneficiary for all purposes under this Section.

(6) This Section shall be applicable only to those trusts as defined in Section 82(a).

(7) This Section shall not be applicable to an increase in compensation requested by a trustee in a proceeding pursuant to Section 15680(b) of the Code.

Section 15661. (New) -

15661(a) A successor trustee shall be selected as follows:

(1) By the method provided in the trust instrument to fill a vacancy in the office of trustee, or to the person named in the trust instrument.

(2) If subsection (1) is not applicable, a successor corporate trustee may be selected by all beneficiaries as defined in Section 15681(b)(5) without confirmation of the court.

(3) If a successor trustee is not selected under subsections (1) or (2), a successor trustee may be selected by all beneficiaries, subject to confirmation of the court.

(4) If all of the beneficiaries cannot agree on the identity of a successor trustee, any interested person may petition the court for appointment of a successor trustee under Section 17200.

15661(b) If the successor trustee is an individual, the terms of Section 15602 shall apply.

Section 16443. Liability for Exemplary Damages

Section 16443. If a breach of trust results from the willful misconduct, fraud, or gross negligence of the trustee, the court may find the trustee liable for an amount of exemplary damages not exceeding three times the amount of liability determined under Section 16440.