

## Memorandum 88-61

Subject: Study L-3010 - Fees of Corporate Trustees (Draft of Tentative Recommendation)

Attached to this memorandum is a staff draft of a tentative recommendation intended to implement Commission decisions made at the July meeting concerning fees of corporate trustees. The draft statute proposes revisions in the Trust Law to clarify the right of the court to review fees, to remove a trustee on petition for an unreasonable increase in fees, and to provide a mechanism for notice of fee increases and beneficiary acceptance or rejection. These are the areas that the Commission decided to pursue at this point in the process.

Several policy issues are discussed in the notes following the relevant sections in the draft statute. Some of these notes reflect matters discussed in the general policy discussions we have had at several meetings in the past. In addition, some new issues are presented in the draft, such as, for example, whether termination fees should be controlled.

At the September meeting, we plan to review the draft statute section by section.

Application of Statute to Individual Trustees

Some bank representatives and others have suggested that any new procedures or standards for review of trustees' fees and any new procedures should apply to both individual and corporate trustees. The draft statute applies the provisions relating to removal for unreasonable fee increases and review of fees to all trustees. It also applies the procedure for giving notice of a fee increase to all trustees, although the staff is not confident that it will work too well with individual trustees, since they are unlikely to have fee schedules.

### Termination Fees

The ability to take advantage of a competitive market is, to some extent, inhibited by the standard charges for winding up the trust with the old trustee and setting up the trust with the new trustee. Our survey of corporate trustees last year found that minimum charges ranged from around \$200 to \$500 and that some charged 1% of the value of trust assets. In addition, most corporate trustees will charge expenses for transferring assets or a set fee such as \$20-\$25 per securities issue and \$75-\$100 for real estate.

In this connection, Delaware law is interesting. Delaware regulates termination and transfer fees depending on how long the trust has been administered by the trustee. The standard fee is reduced by 30% after 3 years and ranges up to a 100% reduction after 9 years. (See Del. Ch. Ct. R. 132(e) in Exhibit 2.) Is the Commission interested in including this type of provision in the tentative recommendation? The declining scale, or a variation of it, could be applied to the termination fee stated by the trustee when the trust was established or as later adjusted.

### Exemplary Damages

The revised California Bankers Association draft proposes a limitation on exemplary damages. (The CBA draft was distributed for the last meeting; another copy is attached as Exhibit 1.) The CBA draft section is essentially the same as a section included in the Trust Law as originally proposed by the Commission. However, the section was opposed by the California Trial Lawyers Association when the bill 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 did not pursue the earlier proposal.

Now this provision is again before us by way of the CBA draft. We have included it in the staff draft attached to this memorandum for the purposes of discussion. 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 has mixed feelings about pushing this provision again, 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

CA LAW REV. COMMISSION

JUN 23 1988

RECEIVED

June 22, 1988

Mr. John H. DeMouilly  
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. DeMouilly:

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.

John DeMouilly  
June 22, 1988  
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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  
Chairman, California Bankers  
Association Trust  
State Governmental Affairs Committee  
(415) 983-3751

DWL:dp

Enclosure

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.

EXHIBIT 2

## DELAWARE CHANCERY COURT RULE 132

## TRUSTEES' FEES

**RULE 132. FIDUCIARY COMMISSIONS**

As used in this rule the terms "trustee" or "trustees" mean testamentary trustees, trustees for mentally ill persons, trustees by appointment of the Court, and other trustees, guardians and fiduciaries whose duties call for the care and management of property (referred to herein as the "trust estate" or the "trust").

As used in this rule the term "commission period" means a period covering 1 month, 3 months, 6 months or a year.

Subject to the provisions of any valid agreement determining compensation, and subject in any case to increase or decrease by the Court for cause appearing sufficient to the Court, a trustee shall be entitled to the following commissions for services:

(a) **Income Commissions.** A charge on gross income during each trust accounting year collected by the trustee calculated at the following rates:

- 6% on the first \$20,000 of income;
- 3.5% on the next \$10,000 of income;
- 3% on the next \$270,000 of income;
- 2% on all income over \$300,000.

(b) **Periodic Principal Commissions.** A charge on the principal or corpus of the trust estate, computable and payable at the times and in the manner hereinafter set forth at the following annual rates:

- $\frac{5}{10}$  of 1% on the first \$100,000 of principal;
- $\frac{3}{10}$  of 1% on the next \$100,000 of principal;
- $\frac{2}{10}$  of 1% on the next \$500,000 of principal;
- $\frac{1}{10}$  of 1% on all principal over \$700,000.

The principal commissions shall be computed for each commission period on the basis of the fair value of the trust estate, which shall be determined either (1) for any commission period less than annually by an appraisal made by the trustee and certified to the Court as of the last business day of the commission period selected; or (2) by the value theretofore determined as a part of a periodic review of trusts by the trustee, such review to be of a date not more than 12 months prior to the date of making such annual charge. Periodic reviews to be eligible for use for valuation purposes under clause (2) shall be made approximately at 12-month intervals and the date of such reviews shall not vary more than 60 days from 1 year to the next until the termination of the trust, as of which date a final valuation shall be made.

Principal received or withdrawn during any commission period shall be included in the total valuation of the trust estate, but, as to commission periods in excess of 3 months, its value shall be adjusted proportionately for each 3-month period in such commission period that preceded the date of its receipt or followed the date of its withdrawal.

A trustee shall, with respect to any particular trust, select 1 of the commission periods permitted by these Rules and shall adhere to the period selected in computing successive periodic principal commissions for that trust; provided that a trustee may thereafter change such commission period upon notice to the beneficiaries of the trust who are then entitled to receive distributions of income or principal, and to any co-trustees or trust advisors for the trust involved. In any periodic accounting which a trustee is required to file under Rule 114, such fair value so computed shall be certified to the Court in the form of written statements by the trustee, 1 for each commission period for which principal commissions are claimed. Each such certification shall contain a complete list of assets of the principal of the trust estate, the amount of the fair value of each asset, a statement showing which of the methods above referred to has been adopted as a basis of the valuation and the date of such valuation.

The charge and collection of principal commissions for 1 or more commission periods may at any time from time to time be deferred; in such case, a notation shall be entered on the account submitted to the Court showing the accumulated amount of such principal commissions as computed but not actually charged.

A trustee may elect not to compute or charge periodic principal commissions in which event the trustee shall, at the time of distribution or of termination of the trust or of transfer to a successor trustee, be allowed principal commissions computed under the provisions of paragraph (e) of this rule, or in lieu thereof the trustee may at such time or times apply to the Court for appropriate commissions on principal, which the Court in its discretion may allow and which need not be limited to the amounts of principal commissions at termination set forth by paragraph (e) of this rule.

Notwithstanding an earlier election not to compute or charge periodic principal commissions, a trustee may elect prospectively to compute, charge and collect such commissions at any time during the administration of the trust estate.

Periodic principal commissions may be collected less frequently than the commission period selected for their computation and charge.

**(c) Additional Charges in Special Cases.** When the trust includes 1 or more mortgages, an additional commission shall be allowed at the annual rate

of  $\frac{1}{4}$  of 1% of the total face value of all mortgages held in the trust as of the times of the valuation of the trust assets required by paragraph (b) of this rule or, if the trustee is not charging periodic principal commissions, of the total face value of such mortgages held in the trust on the last business day of each fiscal year of the trust.

When the trust includes real estate, the income commission specified in paragraph (a) of this rule shall apply to gross rents collected by an outside agent and paid to the trustee. If such rents are collected directly by the trustee, the trustee shall be allowed a commission of 8% of gross rentals received.

In the discretion of the Court, additional and special commissions may be allowed for unusual and extraordinary services.

**(d) Decrease of Commissions in Certain Cases.**

**(1) Control in Person Other Than Trustee.** If the direction and control of investments in any trust, the corpus of which exceeds \$300,000 in value, rest solely with a person other than the trustee, the principal commissions set forth in paragraph (b) of this rule shall be reduced by 15 percent so long as such condition exists. .

**(2) Large Blocks of Securities.** In a trust with limited diversification and a fair value of \$1,000,000 or more, three fourths or more of the fair value of which is invested in not more than 2 blocks of stocks and/or bonds, the income commission set forth in paragraph (a) of this rule shall be reduced by 25 percent, so long as such condition exists.

**(e) Principal Commissions Upon Distribution or Transfer.** Upon partial or complete distribution of any trust, or upon transfer to a successor trustee, the aggregate principal commissions allowable shall be calculated at the following rates:

- 5% of principal on the first \$50,000;
- 3.6% of principal on the next \$50,000;
- 2.3% of principal on the next \$900,000;
- 1% of principal on all over \$1,000,000.

Provided, however, that if at the time of distribution or transfer the trust shall have been administered by the trustee for a period less than 10 years, such principal commissions shall be reduced to the following percentages of the rates hereinabove specified:

- 30% if termination occurs within 3 years;
- 40% if termination occurs after 3 and before 4 years;
- 50% if termination occurs after 4 and before 5 years;
- 60% if termination occurs after 5 and before 6 years;
- 70% if termination occurs after 6 and before 7 years;
- 80% if termination occurs after 7 and before 8 years;
- 90% if termination occurs after 8 and before 9 years;
- 100% if termination occurs after 9 years.

There shall be deducted from such principal commissions the sum of all periodic principal commissions theretofore charged and collected by the trustee with respect to the trust estate or, in the case of a partial distribution, with respect to the distributable portion of the trust estate. If such sum exceeds the aggregate principal commission allowable under this paragraph, the

trustee shall not be obligated to repay such excess but shall not ordinarily be allowed any additional principal commission upon termination of the trust.

Such aggregate principal commission shall be computed on the basis of the fair value of the trust estate at the time of partial or complete distribution or of transfer to a successor trustee. Such fair value shall be determined by an appraisal made by the trustee as of the date of partial or complete distribution or transfer. In any accounting which a trustee is required to file, such fair value so determined shall be certified to the Court in the form of written statements by the trustee filed with and as a part of the final account of the trustee, or in the case of partial distribution or transfer, as a part of the next account of the trustee required under these rules. Each such certification shall contain a complete list of the assets of the principal of the trust estate, the amount of the fair value of each asset, the date of such valuation, and a statement of the amounts previously allowed the trustee as periodic principal commissions under this rule. The time or date of partial or complete distribution or transfer shall mean the date of the event that caused the partial or complete termination or transfer of the trust: e.g., the date a beneficiary dies, the date a beneficiary comes of age, or the date on which a written instrument is delivered to the trustee or a Court order is entered authorizing or directing the transfer to a successor trustee.

**(f) Apportionment of Commissions.** Except to the extent that the governing instrument or a Court order shall otherwise provide, principal commissions shall be paid out of principal and income commissions shall be paid out of income. Additional commissions on mortgages and real estate shall be charged to income.

**(g) Perpetual Trusts.** If a trust is or becomes perpetual (a charitable trust, e.g.), the trustee shall be entitled to the total commissions set forth under paragraphs (a) and (b) of this rule, which shall be charged entirely against income.

**(h) Cotrustees.** The compensation to be allowed to each of 2 or more trustees shall be as the Court in its discretion may determine, considering the amount and character of the trust property, the extent of the risk and responsibility of each trustee, the character of the services rendered by each trustee, the degree of difficulty in administering the trust, the skill and success of the administration, and any other relevant and material circumstances. The compensation allowed each trustee, upon petition of any of them, shall be computed in a manner consistent with the above schedule, but the amounts allowed in the aggregate may exceed the amounts allowed a single trustee at the rates set forth above for normal services.

**(i) Certain Payments Income for Commission Purposes.** For the purpose of determining commissions upon income allowable under this rule, income shall be deemed to include (without being limited to) periodic payments of insurance, annuities, pensions, social security and railroad retirement board benefits and the like, whether received from public, private or governmental sources; provided that payments shall have been received at substantially regular intervals over a period of at least 12 months during the continuance of the trust and provided further that the Court may in its discretion, when the circumstances are such that the allowance of such commissions



upon such payments would work an undue hardship, enter an order modifying the extent to which the provisions of this paragraph shall be applicable to the allowance of commissions on such payments.

**(j) Trustee's Fee for Review of Accountings of an Executor or an Administrator Other than Trustee.** When a trustee receives property from an executor or administrator other than itself, a fee equal to the reasonable costs actually incurred by the trustee shall be charged against principal and allowed to the trustee as compensation for review of the actions, administration and accounting of the executor or administrator. In no event, however, shall this fee exceed the sum of \$1,000 without special allowance of the Court.

**(k) Successor Trustee's Fees for Review of Accountings of Former Trustee.** When a successor trustee receives property from a former trustee, a fee equal to the reasonable costs actually incurred by the successor trustee shall be charged against principal and allowed to the successor trustee as compensation for review of the actions, administration and accounting of the former trustee. In no event, however, shall this fee exceed the sum of \$1,000 without special allowance of the Court.

**(l) Minimum Commissions.** A trustee shall be entitled to a minimum commission of \$400 for services in any 1 accounting year to be charged against income to the extent collectible as computed under paragraph (a) of this rule and the balance, if any, to be charged against principal.

(Amended, effective Jan. 1, 1972; July 1, 1979; Jan. 1, 1983.)

**Cross reference.** — As to commission of trustees under will, see § 3534 of Title 12.

**Court may grant full fees.** — Although this rule provides that trustees' commissions are "subject in any case to increase or decrease by the Court for cause appearing sufficient to the court," the Court is justified in granting full fees if it finds the trustee performed its duties faithfully and well. *Cleveland Trust Co. v. Wilmington Trust Co.*, Del. Supr., 258 A.2d 58 (1969).

**And parol evidence as to trustee's fees may be considered.** — When the provision for a trustee's fees is reasonably susceptible to different meanings, parol evidence as to "pertinent explanatory circumstances" may be considered to resolve the uncertainty and to ascertain the intent of the parties to the trust agree-

ment. *Cleveland Trust Co. v. Wilmington Trust Co.*, Del. Supr., 258 A.2d 58 (1969).

**Unless trust agreement contains unambiguous provision as to amount.** — Where a trust agreement contains a clear and unambiguous provision as to the amount of the fee on principal which would be owing upon transfer of the res to a successor trustee, there is no room for parol evidence as to that issue. *Cleveland Trust Co. v. Wilmington Trust Co.*, Del. Supr., 258 A.2d 58 (1969).

**"Distribution" and "transfer" are distinguished.** — It is clear from this rule that it is customary in banking circles to distinguish between "distribution" to beneficiaries and "transfer" to a successor trustee as words of art. *Cleveland Trust Co. v. Wilmington Trust Co.*, Del. Supr., 258 A.2d 58 (1969).

Staff Draft

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TENTATIVE RECOMMENDATION  
relating to  
TRUSTEES' FEES

BACKGROUND

As compensation for administering the trust, a trustee is entitled to a fee as provided in the trust instrument.<sup>1</sup> The amount specified in the trust is subject to court review and may be reduced where, for example, the amount provided in the trust is inequitable or unreasonably high.<sup>2</sup> If the trust instrument does not set the trustee's compensation, the trustee is entitled to a reasonable fee under the circumstances.<sup>3</sup>

In the past, when testamentary trusts were more closely controlled by the courts,<sup>4</sup> the trustee's fees were subject to review in the annual approval of accounts. Under this scheme, the first bracket

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1. Prob. Code § 15680(a).
  2. Prob. Code § 15680(b). This remedy also applies where the amount of compensation is inadequate and the trustee seeks a higher amount. An order changing compensation acts only prospectively.
  3. Prob. Code § 15681.
  4. Trusts created after 1977 were not subject to continuing jurisdiction, but were made subject to the statute covering living trusts. See Prob. Code § 1120(c), as added by 1976 Cal Stat. ch. 860, § 3. Beginning in 1983, trusts created before July 1, 1977, were required to be removed from continuing jurisdiction, if the trust had a corporate trustee, or permitted to be removed, if the trust did not have a corporate trustee. See Prob. Code § 1120.1a, as added by 1982 Cal. Stat. ch. 1199, § 2. The Trust Law, operative on July 1, 1987, reconfirmed the preference for intermittent court jurisdiction over both testamentary and living trusts at the instigation of an interested person. See Prob. Code § 17209.

percentage fee was typically  $\frac{1}{2}$  of 1% of the principal value of trust property.<sup>5</sup>

Since 1982, many trust companies have increased their first bracket rates to 1% or more.<sup>6</sup> In addition, several trust companies have raised the size of the first bracket so that the highest percentage fee is charged over a greater value of trust property.<sup>7</sup> In most cases, the minimum fee has also been increased.<sup>8</sup>

The Commission has made no judgment on the propriety of the fees charged by California trustees. It has been suggested that the fee increases have resulted from a number of factors, such as inflation, the increased cost of doing business, additional burden of regulation and reporting imposed on the banking industry, and a greater exposure to liability.<sup>9</sup> It has also been suggested that the fees in the past may have been artificially low, but that trust departments are now expected to produce a higher level of return.<sup>10</sup>

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5. See, e.g., Cohan & Fink, *Trustees and Administrative Provisions*, in *California Will Drafting* § 17.23, at 608 (Cal. Cont. Ed. Bar 1965); *California Will Drafting Supplement* § 17.23, at 259-260 (Cal. Cont. Ed. Bar 1981).

6. This conclusion is based on information gathered from 24 California trust companies comparing fee schedules in effect in 1982 and 1987. Ten out of 18 respondents had increased percentage rates during this 5-year period. See *Corporate Trustees' Fees: Summary and Analysis of Information from Corporate Trustees 2-4* (October 1987) (on file at Commission office).

7. Five of the respondents raised the ceiling of the first bracket to which the highest percentage rate is applied. See *Corporate Trustees' Fees: Summary and Analysis of Information from Corporate Trustees 2-6 & data* (October 1987) (on file at Commission office).

8. Fifteen of 18 respondents increased minimum fees between 1982 and 1987. One bank lowered its minimum fee. See *Corporate Trustees' Fees: Summary and Analysis of Information from Corporate Trustees 4-6* (October 1987) (on file at Commission office).

9. See statements of bank trust officers quoted in the appendix to *Corporate Trustees' Fees: Summary and Analysis of Information from Corporate Trustees* (October 1987) (on file at Commission office), at 16-18.

10. *Id.*

RECOMMENDATIONS

The appropriate level of fees for services should continue to be determined by the parties to the trust and not by statute or by requiring court approval of fees. This approach is consistent with modern trust administration under which the interested parties are expected to take the initiative in protecting their rights. The settlor presumably takes the trustee's fee schedule into account in selecting the trustee.<sup>11</sup> In addition, the trust instrument may provide a mechanism for determining fees or replacing a trustee if the fees become excessive without the need to petition the court. After a trust is established, the persons having the power to modify or terminate the trust clearly should have the power to accept or reject fee increases.

The Commission recommends (1) making existing judicial remedies more explicit and (2) adding a new procedure providing for notice of and objection to proposed fee increases.

To implement the first recommendation, the Trust Law should be revised to provide explicitly that the court, on petition of a beneficiary or cotrustee, may review the reasonableness of the trustee's compensation and order a different amount. The grounds for removal of a trustee should also include situations where the trustee's fee is unreasonable under the circumstances.

The second recommendation would be implemented by requiring trustees to give at least 60 days' written notice to the beneficiaries<sup>12</sup> of a proposed increase in percentage or minimum fees. If no beneficiary objects in writing to the proposed fee increase within the 60-day period (or longer period afforded by the trustee),

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11. This recommendation is mainly concerned with irrevocable trusts, whether living or testamentary, since the settlor under a revocable trust may replace the trustee at will in response to an unreasonable fee increase.

12. For this purpose, "beneficiaries" would include all beneficiaries to whom income or principal is required or authorized in the trustee's discretion to be currently distributed under the trust. This is the same class of beneficiaries who are entitled to an account under Probate Code Section 16062.

the proposed fee increase would become effective. If all beneficiaries object to the proposed fee increase and are unable to work out a compromise with the trustee, the beneficiaries could replace the trustee without the need to petition the court. In addition, if all beneficiaries object, the trustee would be permitted to resign without court approval and would not be liable for the resignation or for the selection of, or acts or omissions of, the successor trustee. If one or more, but not all, of the beneficiaries object and the proposed increase is not compromised, the trustee would have to petition the court for an increased fee, or could petition to resign the trust. If the trustee petitions for approval of the fee increase, the court would have discretion to award costs and attorney's fees to be paid out by the trustee, the trust, or the objecting beneficiary, as justice requires.

The proposed legislation would also limit exemplary damages for breach of trust to no more than three times compensatory damages.<sup>13</sup> Although the right to exemplary damages against trustees is not well-established, the traditional reluctance to award such damages is dissipating. Recent cases have indicated a willingness to award exemplary damages against fiduciaries.<sup>14</sup> The potential for large punitive damages awards may act as an incentive for trust companies to raise fees across the board, to the detriment particularly of smaller trusts. Thus it is in the interest of trust beneficiaries as a group to limit the potential liability for exemplary damages. Consequently, the Commission renews its recommendation that exemplary damages for breach of trust involving the trustee's willful misconduct, fraud, or gross negligence may not exceed three times the amount of compensatory damages.

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13. The Commission originally recommended this provision as part of the comprehensive trust bill. See Recommendation Proposing the Trust Law, 18 Cal. L. Revision Comm'n Reports 501, 560, 713 (1986).

14. See *Vale v. Union Bank*, 88 Cal. App. 3d 330, 339-40, 151 Cal. Rptr. 784 (1979); *Werschkull v. United California Bank*, 85 Cal. App. 3d 981, 1000-04, 149 Cal. Rptr. 829 (1978); see also *Schoenholtz v. Doniger*, 657 F. Supp. 899, 913-16 (S.D.N.Y. 1987).

White

The Commission's recommendation would be effective of the following measure:

An act to amend Sections 15642 and 17200 of, to and 16443 to, and to add Article 6 (commencing with Section 15642) to Chapter 1 of Part 3 of Division 9 of, the Probate Code, relating to trusts and trustees.

*The people of the State of California do enact as follows:*

**Probate Code § 15642 (amended). Removal of trustee**

SEC. 1. Section 15642 of the Probate Code is amended to read:

15642. (a) A trustee may be removed in accordance with the trust instrument or by the court on its own motion or on petition of a cotrustee or beneficiary.

(b) The grounds for removal of a trustee by the court include the following:

(1) Where the trustee has committed a breach of the trust.

(2) Where the trustee is insolvent or otherwise unfit to administer the trust.

(3) Where hostility or lack of cooperation among cotrustees impairs the administration of the trust.

(4) Where the trustee fails or declines to act.

(5) Where the trustee's compensation is unreasonable under the circumstances.

(6) For other good cause.

(c) If it appears to the court that trust property or the interests of a beneficiary may suffer loss or injury pending a decision on a petition for removal of a trustee and any appellate review, the court may, on its own motion or on petition of a cotrustee or beneficiary, compel the trustee whose removal is sought to surrender trust property to a cotrustee or to a receiver or temporary trustee. The court may also suspend the powers of the trustee to the extent the court deems necessary.

**Comment.** Paragraph (5) is added to subdivision (b) to make clear that a trustee may be removed by the court where the trustee's compensation is unreasonable under the circumstances. This is a clarification of the law, rather than a new principle. If a trustee is

removed, another trustee may be appointed to fill the vacancy as provided in Section 15660. See also Section 15681 (trustee entitled to reasonable compensation under the circumstances).

*Note.* The new provision is phrased in general terms in order to make the court's authority clear while not being overly restrictive. The provision does not deal with the situation where an objection to the fee increase is not made in a timely fashion as provided in draft Section 15694. It does not present a practical problem, however, since petitions to remove trustees are presumably rare.

**Probate Code § 15661 (added). Selection of successor trustee**

SEC. 2. Section 15661 is added to the Probate Code, to read:

15661. If a trustee resigns pursuant to Section 15695, a successor trustee shall be selected as follows:

(a) If the trust instrument provides a practical method of appointing a successor trustee or names a successor trustee, the successor shall be selected as provided in the trust instrument.

(b) If subdivision (a) is not applicable, a trust company may be selected as successor trustee by agreement of all beneficiaries entitled to notice under Section 15692 without the need for court approval.

(c) If the successor trustee is not selected pursuant to subdivision (a) or (b), the court may appoint a successor trustee on petition of a beneficiary,.

**Comment.** Section 15661 governs selection of a successor trustee to fill the vacancy created by resignation of a trustee pursuant to Section 15695 following a failed attempt to gain approval of a proposed fee increase. Subdivisions (a) and (c) are comparable to subdivisions (b) and (c) of Section 15660.

Subdivision (b) permits the beneficiaries who are entitled to notice under Section 15692 to select the successor trustee without going to court if the trust does not provide a special procedure or name a successor. Subdivision (b) applies only where the successor trustee agreed on by all beneficiaries is a trust company. If the beneficiaries wish to select an individual trustee, court approval must be sought. See Section 17200(b)(10) (petition for appointment of trustee). If the successor trustee is an individual, the bond requirements of Section 15602 may apply.

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**Probate Code §§ 15690-15696 (added). Notice and Review of Fee Increases**

SEC. 3. Article 6 (commencing with Section 15690) is added to Chapter 1 of Part 3 of Division 9 of the Probate Code, to read:

Article 6. Notice and Review of Fee Increases

**§ 15690. "Trustee's fee" defined**

15690. As used in this article, "trustee's fee" means the trustee's periodic base fee, rate of percentage compensation, or minimum fee.

**Comment.** Section 15690 defines "trustee's fee" for the purposes of this article governing increases in base, percentage, and minimum fees. This limited definition does not apply to provisions not in this article.

**Note.** *The CBA draft referred to the "stated" fee. We have omitted this term as being too limiting or vague. The staff believes that the reference to base fees, percentage fees, and minimum fees is sufficiently concrete and descriptive of the subject of this procedure. The procedure should apply to published fees, fees agreed on in the trust, or even fees set by practice.*

**§ 15691. Application of article**

15691. Notwithstanding any provision in the trust, the trustee may increase the trustee's fee only after compliance with this article or pursuant to a court order.

**Comment.** Section 15691 makes clear that the procedure applicable to increases in trustees' fees under this article governs even where the trust instrument contains a contrary provision concerning the trustee's fees. See Section 15690 ("trustee's fee" defined). It should be noted, however, selection of a successor trustee is subject to trust provisions. See Section 15661.

The last clause of this section recognizes that this article does not govern fee increases that are approved by the court. See Sections 15680, 17200(b)(9).

**§ 15692. Notice of proposed fee increase**

15692. (a) If a trustee proposes to increase the trustee's fee, the trustee shall give at least 60 days' written notice of the proposed fee increase to each beneficiary to whom income or principal is required or authorized in the trustee's discretion to be currently distributed under each trust that would be affected by the proposed fee increase. The effective date of the proposed fee increase may be



different from the date by which the trustee is to receive an objection, but at least 60 days shall be allowed for making an objection.

(b) Notice of the proposed increase of the trustee's fee shall include the following information:

(1) A statement that the trustee proposes to increase the trustee's fee.

(2) The effective date of the proposed fee increase.

(3) The trustee's fee currently charged that would be affected by the proposed fee increase and the amount or rate of the proposed fee increase.

(4) The name, address, and telephone number of the trustee or the trustee's representative to whom questions may be addressed and to whom any objections shall be directed.

(5) A statement that the proposed fee increase will become effective on the stated date unless a beneficiary's written objection is received by the designated trustee or trustee's representative within the time allowed for making an objection.

(6) The date by which any objections to the proposed fee increase must be received by the designated trustee or the trustee's representative.

(7) A statement that if an objection is made within the time allowed, the trustee may withdraw the proposed fee increase or seek to compromise the proposed fee increase, may petition the court for approval of the trustee's resignation, or may petition the court for approval of all or part of the proposed fee increase.

(8) A statement that if the trustee successfully petitions for court approval, the objecting beneficiary or the trust may be held liable for the trustee's costs and attorney's fees, and that if the trustee's petition is unsuccessful, the trustee may be held liable for the objecting beneficiary's costs and attorney's fees.

(9) A statement that if all the beneficiaries who are entitled to notice of the proposed fee increase agree in writing, the beneficiaries may replace the trustee with a successor trustee pursuant to Section 15661 or the trustee may resign pursuant to Section 15695.

Comment. Section 15692 requires the trustee to give notice to certain beneficiaries of a proposed fee increase. The class of

beneficiaries entitled to notice under subdivision (a) is drawn from Section 16062 (duty to account). Where the trust is revocable, the settlor has the rights of the beneficiaries. See Section 15800. See also Sections 1003 (guardian ad litem), 15802 (notice to person holding power to revoke), 15803 (rights of holder of power of appointment or withdrawal), 15804 (notice in case involving future interest).

Subdivision (b) sets out the required contents of a notice of proposed fee increase. As to the liability for costs and attorney's fees, see Section 15696.

**§ 15693. Increased fee allowed if no objection**

15693. The trustee may increase the trustee's fee as stated in the notice unless, within the time allowed for making an objection stated in the notice, either of the following occurs:

(a) The trustee receives an objection to the proposed fee increase from any person entitled to notice under Section 15692.

(b) The trustee receives notice of a petition under Section 17200 relating to the proposed fee increase.

**Comment.** Section 15693 provides two circumstances that prevent a proposed fee increase from taking effect according to its terms. An objection, as provided in subdivision (a), is part of the procedure provided by this article. A petition under Section 17200 relating to the trustee's fee takes the matter out of this article and the court has jurisdiction over the fee issue. See Section 17200(b)(9).

**§ 15694. Procedure if beneficiary objects**

15694. If any person entitled to notice under Section 15692 objects to the proposed fee increase by delivering a written notice of the objection to the trustee within the time allowed for making an objection, the proposed fee increase does not become effective and the trustee may do any of the following:

(a) Withdraw the proposed fee increase as to that trust.

(b) Revise the proposed fee increase and give notice of a different proposed fee increase under the procedure provided by this article.

(c) Petition the court for approval of the proposed fee increase or a modified fee increase.

(d) Petition the court to accept the trustee's resignation.

**Comment.** Section 15694 provides for the trustee's options following a timely objection to the proposed fee increase. See Section 15695 (right to resign if all beneficiaries object). See also Section 15696 (liability for costs and attorney's fees).

**§ 15695. Resignation or removal if all beneficiaries object**

15695. (a) If all persons entitled to notice under Section 15692 object in writing to the proposed fee increase within the time allowed, and the proposed fee increase is not compromised or withdrawn, they may, within 60 days after expiration of the time allowed for making an objection, remove the existing trustee without obtaining court approval and select a successor trustee as provided in Section 15661.

(b) If all persons entitled to notice under Section 15692 object in writing to the proposed fee increase within the time allowed, the trustee may, within 60 days after expiration of the time allowed for making an objection, resign as trustee without obtaining court approval. The trustee's resignation under this subdivision is not effective until a successor trustee is selected.

(c) A trustee who is removed or resigns pursuant to this section is not liable for any consequences of the resignation and is not liable for the selection of, or the acts or omissions of, the successor trustee.

**Comment.** Section 15695 gives the trustee the right to resign as trustee and permits the removal of the trustee without court approval if all the persons entitled to notice object to the fee increase in writing. If fewer than all such persons object, the trustee would have to petition the court to permit the resignation or the objecting beneficiaries would have to petition for removal of the trustee, if they so desire. See Section 15694 (procedure if beneficiary objects).

**§ 15696. Liability for costs and attorney's fees**

15696. If the trustee petitions for approval of all or part of the proposed fee increase under Section 15694, the court may, in its discretion, order costs and attorney's fees to be paid by the trustee, the trust, or the beneficiary who objected to the proposed fee increase, as justice may require. If the objecting beneficiary is made liable for costs or attorney's fees, the amount may be charged against the beneficiary's interest in the trust, as ordered by the court.

**Comment.** Section 15696 gives the court authority to award costs and attorney's fees in the interests of justice.

**Probate Code § 16443 (new). Liability for exemplary damages**

SEC. 4. Section 16443 is added to the Probate Code, to read:

16443. If a breach of trust results from the trustee's willful misconduct, fraud, or gross negligence, 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.

**Comment.** Section 16443 is new and is intended to clarify the right to exemplary damages for breach of trust. This section codifies the right to exemplary damages found in some appellate cases. See *Vale v. Union Bank*, 88 Cal. App. 3d 330, 339-40, 151 Cal. Rptr. 784 (1979); *Werschull v. United California Bank*, 85 Cal. App. 3d 981, 1000-04, 149 Cal. Rptr. 829 (1978); see also *Schoenholtz v. Doniger*, 657 F. Supp. 899, 913-16 (S.D.N.Y. 1987).

**Probate Code § 17200 (amended). Petitions; grounds for petition**

SEC. 5. Section 17200 of the Probate Code is amended to read:

17200. (a) Except as provided in Section 15800, a trustee or beneficiary of a trust may petition the court under this chapter concerning the internal affairs of the trust or to determine the existence of the trust.

(b) Proceedings concerning the internal affairs of a trust include, but are not limited to, proceedings for any of the following purposes:

- (1) Determining questions of construction of a trust instrument.
- (2) Determining the existence or nonexistence of any immunity, power, privilege, duty, or right.
- (3) Determining the validity of a trust provision.
- (4) Ascertaining beneficiaries and determining to whom property shall pass or be delivered upon final or partial termination of the trust, to the extent the determination is not made by the trust instrument.
- (5) Settling the accounts and passing upon the acts of the trustee, including the exercise of discretionary powers.
- (6) Instructing the trustee.
- (7) Compelling the trustee to report information about the trust or account to the beneficiary, if (A) the trustee has failed to submit a requested report or account within 60 days after written request of the beneficiary and (B) no report or account has been made within six months preceding the request.

- (8) Granting powers to the trustee.
- (9) Fixing or allowing payment of the trustee's compensation or reviewing the reasonableness of the trustee's compensation.
- (10) Appointing or removing a trustee.
- (11) Accepting the resignation of a trustee.
- (12) Compelling redress of a breach of the trust by any available remedy.
- (13) Approving or directing the modification or termination of the trust.
- (14) Approving or directing the combination or division of trusts.
- (15) Amending or conforming the trust instrument in the manner required to qualify a decedent's estate for the charitable estate tax deduction under federal law, including the addition of mandatory governing instrument requirements for a charitable remainder trust as required by final regulations and rulings of the United States Internal Revenue Service, in any case in which all parties interested in the trust have submitted written agreement to the proposed changes or written disclaimer of interest.
- (16) Authorizing or directing transfer of a trust or trust property to or from another jurisdiction.
- (17) Directing transfer of a testamentary trust subject to continuing court jurisdiction from one county to another.
- (18) Approving removal of a testamentary trust from continuing court jurisdiction.
- (19) Reforming or excusing compliance with the governing instrument of an organization pursuant to Section 16105.

Comment. Subdivision (b)(9) of Section 17200 is amended to make clear that the reasonableness of the trustee's compensation is subject to review on petition under this section. This revision is a clarification of, and not a substantive change in, prior law.

Note. We have not dealt with the question of what happens where a beneficiary who did not object after receiving notice of a proposed fee increase files a petition for review of the increase after the time allowed by draft Section 15693. Normal principles of estoppel should be sufficient to permit the court to throw the petition out if it is too soon after the failure to object. However, the failure to object should not bar review on petition of a nonobjector for too long, assuming that the sufficient grounds for revising the fee are shown.