

## Memorandum 89-2

Subject: Study L-3010 - Trustees' Fees (Comments on Tentative Recommendation )

This memorandum considers comments we have received on the *Tentative Recommendation Relating to Trustees' Fees* (October 1988), a copy of which is attached. After considering the issues raised in the notes following various sections in the tentative recommendation, the Commission should be in a position to approve the recommendation for printing and introduction of a bill in the 1989 legislative session.

To date, we have received 10 letters directed toward this recommendation. Copies of the letters are set out on yellow paper in the attached Exhibits. Comments concerning specific provisions in the tentative recommendation are discussed in the notes following the relevant sections.

Four persons approved the tentative recommendation without further comment: Jerome Sapiro of San Francisco (Exhibits p. 1), Wilbur L. Coats of Poway (Exhibits p. 6), Robert J. Berton of San Diego (a former Commission Chairperson) (Exhibits p. 8), and Henry Angerbauer of Concord (Exhibits p. 11).

The tentative recommendation contains four related proposals and the commentary varies depending on the proposal:

§ 15642. Removal of trustee where compensation is excessive

Russell G. Allen of Newport Beach (Exhibits p. 9) supports this provision, while Anne Steele of San Bruno (Exhibits pp.2-3) opposes it.

§§ 15690-15698. Notice and review of fee increases

Several commentators oppose all or part of the proposed nonjudicial procedure for giving beneficiaries a right to consent or object to proposed fee increases.

The California Bankers Association has "significant objections" and "will oppose the Commission's proposed statute in its current

form." (Exhibits p. 14.) CBA's main objections relate to the power of one beneficiary to forestall a fee increase or force the issue into court and the types of fees that are subject to the mandatory procedure.

Paul Gordon Hoffman of Los Angeles (Exhibits p. 7) and Russell G. Allen of Newport Beach (Exhibits pp. 9-10) oppose the proposed procedure, and instead would rely on judicial remedies initiated by objectors.

§ 16443. Treble damages cap on exemplary damages

Russell G. Allen of Newport Beach (Exhibits p. 10) opposes this section on the grounds that it is undesirable to give statutory recognition to exemplary damages against trustees for breach of trust. Mr. Allen considers the deletion of this provision from the trust bill in 1986 to be "the most beneficial change to the proposed law made during the course of the legislative process."

§ 17200. Court review of reasonableness of trustee's fee

In connection with the reasonable fee approach of trust law, Neil S. Bezaire of San Marino (Exhibits pp. 4-5) recommends adoption of a statutory fee schedule like that applicable to probate fees. In support, Mr. Bezaire cites the reasons given by the Commission for keeping the percentage statutory fee in probate.

These matters are discussed in detail in the notes following the relevant provisions in the attached tentative recommendation.

Respectfully submitted,

Stan G. Ulrich  
Staff Counsel

**JEROME SAPIRO**  
ATTORNEY AT LAW  
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CA LAW REV. COMM'N

**NOV 10 1988**

**R E C E I V E D**

Nov. 9, 1988

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, CA, 94303-4739

Re: Tentative Recommendation  
Relating to Trustee's Fees  
#L-3010      Oct. 1988

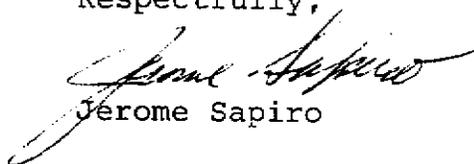
Hon. Commissioners:

The above-mentioned tentative recommendation is approved.

It has been good to participate.

Thank you.

Respectfully,

  
Jerome Sapiro

JS:mes

ANNE STEELE  
ATTORNEY AT LAW  
458 SAN MATEO AVENUE, SUITE 2  
SAN BRUNO, CALIFORNIA 94066  
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CLERK OF SUPERIOR COURT  
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November 9, 1988

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, California 94303-4739

Re: Proposals regarding Trustee's Fees

To the Members of the Commission:

In reviewing your tentative recommendations regarding trustee's fees, I find there to be a continuing uncertainty as to the appropriate amount of fees that are not to be deemed excessive. On the one hand you state that the appropriate level of fees should be determined by the parties to the trust and on the other hand you put forth amendments to remove a trustee for "excessive" fees.

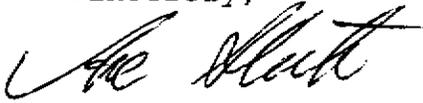
If the parties are free to bargain for fees, then, by definition, the agreed level of fees should be appropriate and not excessive. Such circumstances as a long-time relationship with the trustee, a particular bias or predilection of the trustee, or an incentive to manage a trust that represents an unusual responsibility or anticipated decreasing corpus might necessitate the Settlor of a trust agreeing to pay much higher fees than normal. Just because a fee works out to be 2%, 3%, 4%, or higher, even when someone else is around who would charge less, does not mean that the fees are excessive.

If every trustee must anticipate a challenge from beneficiaries who only want to see part of the total picture and a review by a court which has nothing beyond experience to guide it, fees beyond those previously allowed or currently charged in the community are likely to always be held to be "excessive". Of course, if a particular trustee is removed for such a reason, it might even thwart the intentions of the Settlor.

California Law Revisions Commission  
November 9, 1988  
Page Two

I would suggest a provision that allows a specific written agreement as to the amount or rate of fees to control. This would both stabilize the situation as well as foreclose unwarranted conclusions.

Sincerely,

A handwritten signature in cursive script, appearing to read "Anne Steele".

ANNE STEELE  
AS:ld

  
**BEZAIRE**  
 Law Offices  
 A Professional  
 Corporation

CALIFORNIA LAW REV. COMM'N

NOV 17 1988

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San Gabriel Valley  
 San Fernando Valley  
 Orange County  
 Westside  
 South Bay  
 Long Beach  
 Glendale

November 9, 1988

California Law Revision Commission  
 4000 Middlefield Road, Suite D-2  
 Palo Alto, CA 94303-4739

**Re: Tentative Recommendation Relating to Trustee's Fees**

Gentlemen:

When a settlor sets up a revocable living trust, he or she generally continues handling his or her affairs pretty much the way the settlor did before the trust was set up. The only real difference is that now all of the assets are titled in the name of the settlor as trustee of the trust.

When the settlor dies, there is work that needs to be done similar to that of a probate. The main difference is that there is no court supervision.

Some of the basic steps in settling a trust estate are, as follows:

1. Marshaling of the assets and preparation of an inventory;
2. Making post mortem planning elections such as disclaimers and allocation of assets;
3. Filing of income tax returns, state and federal;
4. Filing of estate tax returns;
5. Having the property appraised to document the stepped-up basis and allocation of assets;
6. Distribution of assets or re-registering of assets in the name of the successor trustee;
7. Notice and accounting.

In reading the tentative recommendations, I was left with the impression that the fees would be the same year after year without consideration that during the first year there will be substantially much more work than the annual accounting.

Over the years, we have been advising our clients that a fair fee for the trustee for settling a trust estate would be 1% of the first million, 3/4 of 1% of the next two million, and 1/2 of 1% of all over that, and we have been basing our fees along the same line.

We think that the reasons given by the Law Revision Commission for maintaining a percentage statutory fee schedule for probate estates applies to trust as well. A percentage fee takes into consideration the responsibility assumed, complexity of the matter, and enables the attorney to handle all trust matters even the small estates. The clients seem to prefer the certainty of the percentage arrangement rather than an open ended hourly rate. The percentage fee also encourages the trustee and the attorney to work quickly and efficiently rather than stringing it out on an hourly basis.

**SUMMARY:**

I think, therefore, that a percentage fee arrangement for settling the trust estate is preferable to an open end "reasonable fee".

Thank you for this opportunity of sharing my thoughts with you.

Sincerely yours,



NEIL S. BEZAIRE

**WILBUR L. COATS**  
ATTORNEY AND COUNSELOR AT LAW

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TELEPHONE (619) 748-6512

November 10, 1988

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, Ca 94303-4739

In re: Tentative Recommendation NOTICE TO CREDITORS  
and TRUSTEES' FEES

Gentlemen:

I approve comments and recommendations as to TRUSTEES' FEES.

The following is suggested for inclusion in NOTICE TO CREDITORS.

Some protection to be provided for the Personal Representative if an action is brought that requires the Personal Representative to defend and the Personal Representative prevails.

I can envision an action that might be settled by agreement or other means whereby it is clear the Personal Representative met all the statutory notice requirements but was still out personal funds to defend an action which had no real merit.

The notice requirement as being set forth is liable to be a mine field for Personal Representatives that do not have a reasonably close relationship with the decedents personal transactions. Some protection should be provided for frivolous actions brought by would be creditors.

Very truly yours,

*Wilbur L. Coats*  
Wilbur L. Coats

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SABBAN &  
BRUCKER

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November 10, 1988

California Law Revision Commission  
4000 Middlefield Road  
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Palo Alto, California 94303-4739

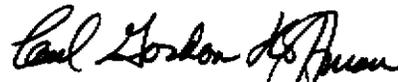
Re: Tentative Recommendation Relating to  
Trustees Fees

Ladies and Gentlemen:

I oppose the portion of the above noted recommendation under which the beneficiaries could replace the trustee simply by objecting to a proposed fee increase. Trusts are often established because the settlor does not trust the beneficiaries to administer the property themselves, and the settlor instead has confidence in the designated trustee. It is not unusual to see hostility between beneficiaries and the trustee in such situations. You can naturally expect opposition from the beneficiaries to any proposed fee increase in an effort to dislodge the trustee and obtain a more pliable administrator.

Where the beneficiaries all oppose the proposed fee increase, their sole remedy should be to seek court review of the proposed increase. If the court finds that the proposed increase is reasonable, then the trustee should be allowed to receive the higher fee regardless of the views of the beneficiaries.

Very truly yours,



Paul Gordon Hoffman

PGH:sc  
P11

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| DENNIS HUGH MCKEE       | KENNETH J. ROSE             |
| JOHN C. HALUGEN         | ERIC B. SHWISBERG           |
| FREDERICK K. KUNZEL     | GERALD P. KENNEDY           |
| ROBERT G. RUSSELL, JR.  | JILL T. AARON               |
| GEORGE L. DAMOOSE       | DAVID A. NIDDIE             |
| KELLY M. EDWARDS        | JEFFREY D. CAWDREY          |
| ANTONIA E. MARTIN       | LYNNE R. LASRY              |
| RAYMOND G. WRIGHT       | DAVID S. GORDON             |
| JAMES G. SANDLER        | KENNETH J. WITHERSPOON      |
| MICHAEL J. RADFORD      | JOSEPH A. HAYES             |
| THOMAS R. LAUBE         | EDWARD I. SILVERMAN         |
| PHILIP J. GIACINTI, JR. | CYNDY DAY-WILSON            |
| STEVEN J. UNTIEDT       |                             |

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A. T. PROCOPIO  
1900-1974

HARRY HARGREAVES  
RETIRED  
JOHN H. GARRETT  
RETIRED

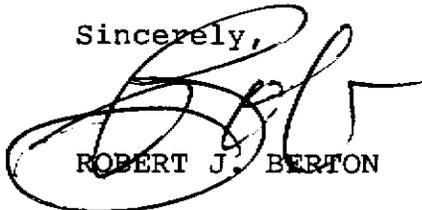
November 15, 1988

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

Dear John:

I support the California Law Revision Commission's  
Tentative Recommendation relating to Trustees' Fees dated  
October 1988.

Sincerely,



ROBERT J. BERTON

RJB:jb

EXCERPT

SUITE 1700  
610 NEWPORT CENTER DRIVE  
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CA LAW REV. COMMISSION  
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November 23, 1988

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, California 94303-4739

Dear Ladies and Gentlemen:

I have comments about several recently-issued tentative recommendations that I wish to submit for your consideration.

Trustees' Fees

While I agree with the proposed change to Section 15642 of the Probate Code to permit a settlor to seek the removal of a trustee and provide that a trustee is removable if the trustee's compensation is excessive, I do not agree with the proposed structure of notice and review of fee increases.

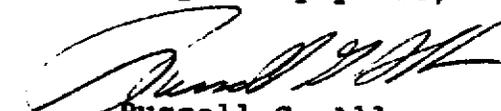
The proposed system reflects the way in which many corporate fiduciaries compute their trustees' fees. While one could debate the desirability of determining trustees' fees (as corporate fiduciaries usually do) based primarily on a percentage of asset value, percentage of income, number of receipts or disbursements, or number of investments held, any further treatment in the trust law concerning trustees' fees, the proposal should contemplate a fee basis that considers other factors that more commonly may be considered by individual trustees. I submit that individual trustees, in particular, often consider family relationship, investment performance, amount of time required, tax consequences, and probably a number of other factors that do not immediately leap to mind. The proposed Sections 15690-15698 do not fit comfortably with these other criteria for reasonableness of trustees' fees. Although I realize it would be more helpful if I proposed an alternative formulation, for the moment I am

inclined to suggest that these new proposed sections be deleted from the overall recommendation. (Indeed, it is not obvious to me that anything more than a statement of the amount of trustees' fees paid over some relatively current period of time is necessary. For trusts recently established, the Code already requires disclosure of that information as a part of the periodic account.)

I also question the desirability of the plan to allow all beneficiaries to remove a trustee who wishes to increase compensation and replace that trustee with a trust company without court intervention. The settlor may pick a fiduciary for a number of reasons, only one of which may be compensation. While I support the right of the beneficiaries to seek judicial removal and replacement of a trustee, I submit that allowing the beneficiaries to proceed without court intervention effectively removes any check to protect the purpose or purposes of the trust relationship as contemplated by the settlor. In my own experience, I have found some settlors to be particularly paternalistic in ways not appreciated by the beneficiaries. Although I believe this is more often true with individual trustees than with corporate trustees, that has not always been the case.

I oppose enactment of the proposed Section 16443 allowing a liability for exemplary damages limited to three times the amount of actual damages. In any particular instance, policy decisions of corporate fiduciaries and the exercise of discretionary decisions with respect to the administration of individual trusts by corporate fiduciaries is not likely to be affected dramatically by the potential award of exemplary damages in addition to an award of actual damages plus the unfavorable publicity that often attends a breach of trust finding. Overall, however, trustees likely will (and I would argue should) seek (depending on the competitive pressures of the marketplace) higher fees because of the greater financial risk involved. As for individual trustees, I think it is much more likely that we will discourage persons from serving (or continuing to serve) as trustee of "difficult" or "messy" situations if they risk an award of exemplary damages. Notwithstanding the Vale and Werschull pension plan cases, I think amending the Code to admit the possibility of exemplary damages for breach of trust is a serious mistake. Deletion of the proposed section by the legislature during its consideration of the trust law -- though perhaps motivated by concern about the limit on liability on the part of some members of the plaintiffs' bar -- was the most beneficial change to the proposed law made during the course of the legislative process.

Very truly yours,

  
Russell G. Allen

RGA/br

HENRY ANGERBAUER, CPA  
4401 WILLOW GLEN CT.  
CONCORD, CA 94521

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11/23/88

California Law Revision Commission:

I have read your tentative recommendations related to Trustees' fees and Compensation of Estate Attorney and Personal Representative. I agree with your recommendations and conclusions and suggest you propose them to the legislature to be implemented into law. Thank you for permitting me to help you in connection with these issues.

Sincerely,  
He

## LATHAM &amp; WATKINS

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CABLE ADDRESS LATHWAT

December 2, 1988

DEC 07 1988

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WASHINGTON, D.C. 20004-2505  
TELEPHONE (202) 637-2200  
TELECOPIER (202) 637-2201Stan G. Ulrich, Staff Counsel  
California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, California 94303-4739Re: Study L-3010: Tentative Recommendation  
Relating to Trustee' Fees

Dear Stan:

I believe I have spotted a potential problem in proposed Probate Code Section 15697. Proposed Section 15697 provides, in substance, that if, within the time allowed for making an objection (as set under Section 15692), all beneficiaries entitled to notice object to the trustee's proposed fee increase in the manner required, the beneficiaries, acting together, may remove the trustee and select a successor trustee, provided they act within 60 days after the expiration of the time allowed for making the objection. This removal right is subject to the limitation that the trustee may not be removed if: "before the expiration of the time allowed for making an objection, the trustee petitions the court for approval of the fee increase or withdraws the proposed fee increase." I would suggest that the underlined phrase be replaced with the following: "within ten days after the expiration of the time allowed for making an objection."

I am concerned with avoiding a situation where one or more disgruntled beneficiaries could abuse this process by using the fee "dispute" as a pretext to oust a corporate or individual trustee imposing appropriate controls. It appears to me that the language now proposed would allow the objecting beneficiaries to wait until the last hour of the notice period provided under Section 15692 and deliver their objections to the trustee. By waiting until the last

Stan G. Ulrich, Staff Counsel  
December 2, 1988  
Page 2

moment, the beneficiaries could effectively cut off the trustee's option to avoid removal under this new section. To avoid such a tactic, it would seem appropriate to provide the trustee some period of time following the expiration of the initial notice period in which to respond to the beneficiaries' timely objections, either by a petition to the court or by the withdrawal of its fee request.

Thank you for your consideration of this comment.

Very truly yours,



Michael S. Whalen  
of LATHAM & WATKINS



California Bankers Association

Trust Financial Services Group

CA LAW REV. COMM'N

December 2, 1988

DEC 08 1988

R E C E I V E D

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

**Re: Trustee Fees (Memorandum 88-77)**

Dear Mr. DeMouilly:

The California Bankers Association has reviewed Memorandum 88-77 which includes a Tentative Recommendation concerning fees of trustees and which was discussed at the October 24, 1988 meeting of the Law Revision Commission. As we previously commented in a letter to you of September 1, 1988, and as representatives of the CBA have stated at the Commission's meetings, the CBA has significant objections to the Commission's proposals. The CBA must state again that it will oppose the Commission's proposed statute in its current form as set forth in Memorandum 88-77.

The major concerns of the CBA, but by no means the only ones, involve two major aspects of the proposed statute. A more detailed letter from the CBA analyzing other issues raised by the Staff proposal will be forwarded separately to the Commission. The two major concerns may be summarized as follows:

1. As we previously commented in our letter to you of September 1, 1988, the proposal at Sections 15693 and 15694 gives one beneficiary the ability to block a fee increase and force either a petition to the court or a resignation of the trustee. In many instances, one beneficiary may be in disagreement with, or have conflicting interests to, other beneficiaries. These provisions would allow a single disgruntled beneficiary to force a trustee to file a court petition or resign even if all other beneficiaries felt that the change in fees was reasonable. Furthermore, this procedure empowers one beneficiary to interfere with the proper administration of the trust by creating an unreasonable burden on the trustee to file such a petition.



California Bankers Association  
Established 1891

Mr. John H. DeMouilly  
December 2, 1988  
Page 2

The CBA continues to believe that all beneficiaries should object to a proposed fee increase in order to trigger the new and dramatic rights given to beneficiaries under the statute. However, in order to suggest a workable and equitable solution, we propose as a compromise that more than 50% of both categories of beneficiaries, as that term is defined in Section 15692(a) of the proposal, must object. The statute would then provide that more than 50% of those beneficiaries "to whom income or principal is required or authorized in the trustee's discretion to be currently distributed" and more than 50% of those beneficiaries who would "receive distribution of principal if the trust were terminated when notice is given" must object in order to trigger the notice provision of the statute. We believe that this concept would be equitable to both categories of beneficiaries and would not favor one category over another, as is potentially the case in the current Staff proposal.

2. We strongly object to the unwarranted expansion of the definition of "Trustee's fees" by the the inclusion of "transaction charges" and "hourly rates". It is inappropriate to include charges for deed preparation, stock sales and other services as referenced in the Staff comment to Section 15690 since the original concern expressed centered on minimum fees and ad valorem percentage fees.

In addition, the drastic remedies given to beneficiaries under the proposed statute should not be triggered by increases in fees for transaction-based charges. The provision of Section 15691(b) is inappropriate and illogical since a relatively small increase in charges for a particular transaction would trigger the notice provisions of the statute. A ten dollar increase from \$75 to \$85 for preparing a deed, for example, would require notices to beneficiaries, a 60 day waiting period, the ability to change trustees, as well as all remedies under the statute. It appears obvious to the CBA that this result is not appropriate for this type of minor increase.



California Bankers Association  
Established 1891

Mr. John H. DeMouilly  
December 2, 1988  
Page 3

Consistent with the foregoing, we suggest the following definition of trustee fee:

"'Trustee's fee' means the compensation for the trustee's ordinary services, whether imposed by a periodic base fee, rate of percentage compensation, or minimum fee."

We further suggest that the de minimis concept applied to transaction charges in the current Staff proposal be rewritten to apply to increases to Trustee's fee as defined above. Accordingly, Section 15691(b) should be rewritten to allow a certain level of increase to trustee's fees without triggering the notice and other provisions of the statute. Such an increase tied to a relatively small percentage change would allow trustees to receive increases to their fees in recognition of ongoing inflationary trends and costly increased regulatory and compliance requirements. In addition, a trustee would be entitled to increase its fees on a cumulative basis and not lose the de minimis increase amount provided in the statute by not increasing fees in any one year. The following is suggested:

"(b) The requirement of subdivision (a) does not apply to any increase in a Trustee's fee that is no greater than 10% per year, calculated on a cumulative basis."

The CBA will have representatives from several California banks present at the January 1989 meeting. We remain committed to working with the Commission and again request the Commission to reevaluate the earlier proposal made by the CBA together with the suggestions contained in this letter.

Very truly yours,

*David W. Lauer*

David W. Lauer  
Chairman, California Bankers Association  
Trust State Governmental Affairs Committee  
(415) 983-3751

DWL/clc

STATE OF CALIFORNIA  
California Law Revision Commission

TENTATIVE RECOMMENDATION

*relating to*

TRUSTEES' FEES

*With Notes on Comments  
Received from Interested Persons*

*As Distributed*

October 1988

CALIFORNIA LAW REVISION COMMISSION  
4000 Middlefield Road, Suite D-2  
Palo Alto, CA 94303-4739

10/24/88

LETTER OF TRANSMITTAL

This tentative recommendation proposes several revisions of the Trust Law (Prob. Code §§ 15000-18201) to provide some control on potential increases in trustees' fees:

(1) The power of the court to review a trustee's fee is made more explicit.

(2) The power of the court to remove a trustee where the trustee's compensation is excessive under the circumstances is also clarified.

(3) A detailed procedure for giving notice of a proposed fee increase to beneficiaries is proposed. It allows for an increase in fees without the need to seek court approval if no timely objection is received from a beneficiary. If an objection is made, the matter may be taken to court or the trustee may resign under certain circumstances.

(4) The right to exemplary damages for breach of trust is given statutory recognition. However, in recognition of the upward pressure on fees that is caused by the potential liability for exemplary damages, this liability would be limited to a maximum of three times actual damages.

The recommendation would also revise the law to permit removal of a trustee of an irrevocable living trust on petition of the settlor.

The Trust Law was enacted on Commission recommendation in 1986. This tentative recommendation relating to trustees' fees is part of the Commission's ongoing effort to review suggestions for improvement in legislation enacted on Commission recommendation.

## TRUSTEES' FEES

Background

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

- 
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.
  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 259-60 (Cal. Cont. Ed. Bar 1981).

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, the 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>

#### 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

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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 & supporting 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 16-18 (October 1987) (on file at Commission office).

10. *Id.*

expected to take the initiative in protecting their rights. The settlor presumably may take 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 nonjudicial procedure providing for notice of and an opportunity to object 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 excessive under the circumstances.

The second recommendation would be implemented by requiring trustees to give at least 60 days' written notice of a proposed fee increase to the trust beneficiaries.<sup>12</sup> The trustee would not be permitted to increase its periodic base fee, rate of percentage compensation, minimum fee, or hourly rate, or to increase transaction charges by 10% or more per year, without following this procedure or petitioning for court approval. If no beneficiary objects in writing to the proposed fee increase within the 60-day period (or longer period

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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 and to those who would receive a distribution of principal if the trust were terminated at the time notice is given. This class of beneficiaries is drawn from Probate Code Section 16062 governing consent to a trustee's resignation. In the case of a minor for whom a guardian has not been appointed, notice would go to the custodial parent, who would then have the right to object under the proposed procedure.

afforded by the trustee), 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, 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 by the trustee, the trust, or the objecting beneficiary, as justice requires.

#### EXEMPLARY DAMAGES

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 for breach of fiduciary duties.<sup>14</sup> The potential for large exemplary damages awards may act as an incentive for trust companies to raise fees across the board, to the detriment particularly of smaller trusts. The exposure to exemplary damages would also make private trustees less willing to serve. Thus it is in the interest of trust beneficiaries as a group to limit the potential liability for exemplary 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); *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).

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.<sup>15</sup>

#### SETTLOR'S PETITION FOR REMOVAL OF TRUSTEE

Traditionally, the settlor of an irrevocable living trust has not been considered to have a sufficient interest in the trust to petition for removal of a trustee, unless such a power is reserved in the trust instrument.<sup>16</sup> If the settlor had or retained an unrestricted power to

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15. Many statutes provide limitations on exemplary damages or set a penalty in a given amount, subject to a ceiling, or as a multiple of actual damages. See Bus. & Prof. Code § 17536 (up to \$2500 for false and misleading advertising); Civil Code §§ 52 (\$250 penalty for violation of Unruh Civil Rights Act), 536 (treble damages for injury to property of cable television corporation), 1710.1 (\$500 penalty plus treble damages for sale of mechanical and electrical appliances with removed or damaged manufacturer's mark or serial number), 1716 (treble damages for solicitation of money for goods not ordered or services not performed), 1719 (treble damages for dishonored check), 1721 (treble damages for malicious destruction of materials at construction site), 1739.4 (treble damages for misrepresentation concerning political campaign items), 1748.1 (treble damages for imposition of surcharge on use of credit card), 1812.123 (treble damages for discount buying services contracts), 1882.2 (treble damages for diversion of utility services), 3346 (treble damages for injury or removal of timber), 3370.1 (up to \$2500 for unfair competition); Code Civ. Proc. §§ 732 (treble damages for waste), 733 (treble damages for injury or removal of timber), 735 (treble damages for forcible or unlawful entry), 1029.8 (treble damages for provision of goods or services by unlicensed persons), 1174(b) (treble damages for forcible entry or unlawful detainer with malice); Food & Agric. Code § 21855 (penalty of four times value plus punitive damages for taking or killing cattle without owner's consent); Labor Code § 1054 (treble damages for preventing employment of former employee, etc.); Penal Code §§ 496 (treble damages plus costs and fees for receiving or concealing stolen property), 637.2 (\$3000 or treble damages for invasion of privacy); Prob. Code §§ 13110 (three times property value for fraudulently securing payment, delivery, or transfer of personal property under affidavit procedure), 13205 (three times property value for execution or filing fraudulent affidavit for disposition of real property of small value).

16. See, e.g., G. Bogert & G. Bogert, Handbook of the Law of Trusts § 160, at 575 (5th ed. 1973).

replace the trustee, the trust would be taxable in the settlor's estate.<sup>17</sup>

The Commission recommends that the settlor of an irrevocable living trust be given the limited power to petition the court for removal of a trustee, on the same footing as a beneficiary or cotrustee.<sup>18</sup> The settlor may be in a good position to assess whether the trustee is failing to administer the trust appropriately. The power to petition for removal would be particularly useful in a case where the settlor has created the trust for minor children, and thus would avoid the need to seek appointment of a guardian ad litem to represent their interests. A statutory right to petition for removal would not have adverse tax consequences because the power to remove the trustee remains in the court's discretion subject to a set of standards.

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17. See E. Depper & A. Bernstein, California Trust Administration § 13.11, at 554 (Cal. Cont. Ed. Bar 1986); Treas. Reg. § 20.2041-1(b)(1) (19 ).

18. See Prob. Code § 15642.

The Commission's recommendation would be effectuated by enactment of the following measure:

An act to amend Sections 15642 and 17200 of, to add Section 16443 to, and to add Article 6 (commencing with Section 15690) 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**

SECTION 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 settlor, 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 excessive 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.** Subdivision (a) is amended to provide the settlor of an irrevocable living trust the right to petition under this section for removal of a trustee. As to the rights of a settlor of a revocable trust, see Sections 15401 (revocation by settlor), 15402 (modification by settlor of revocable trust), 15800 (rights of person holding power of revocation). The right to petition under this section does not give

the settlor any other rights, such as the right to an account or to receive information concerning administration of the trust.

Paragraph (5) is added to subdivision (b) to make clear that a trustee may be removed in the court's discretion where the trustee's compensation is excessive 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.* Russell G. Allen of Newport Beach (Exhibits p. 9) supports the revision of this section.

Anne Steele of San Bruno (Exhibits pp.2-3) opposes it on the grounds that the settlor and the trustee should be able to set the fees without the fear that a court may later remove the trustee for "excessive fees" under this provision. She argues that a community standard might be inappropriately applied to find fees excessive and that removal of the trustee in this type of situation could "thwart the intentions of the settlor." Ms. Steele would make a specific written agreement controlling as to the amount or rate of fees.

The staff does not disagree with the points made by Ms. Steele. An agreement on the fees between the settlor and the trustee should control, assuming that the duties remain essentially the same. This is the intent of Section 15680 which provides that "if the trust instrument provides for the trustee's compensation, the trustee is entitled to be compensated in accordance with the trust instrument." However, it has long been the law that the trustee can receive greater compensation where the duties are greater or where the compensation in the trust is unreasonably low. In the interest of mutuality, the same principles apply where the duties are substantially less than anticipated or where the compensation in the trust instrument is unreasonably high. Ms. Steele's remarks would be more appropriately directed toward these provisions. The standard for removal of a trustee in proposed Section 15642(b)(5) is intended to be stricter than the standard for review under Section 15680. The staff does not believe it is appropriate to revise Section 15680, but it would be useful to add a cross-reference to Section 15680 at the end of the comment to Section 15642.

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#### Probate Code §§ 15690-15698 (added). Notice and Review of Fee Increases

SEC. 2. 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

*Note.* Russell G. Allen of Newport Beach (Exhibits pp. 9-10) would delete this entire article. He writes that

individual trustees, in particular, often consider family relationship, investment performance, amount of time required, tax consequences, and probably a number of other factors that do not immediately leap to mind. The proposed

Sections 15690-15698 do not fit comfortably with these other criteria for reasonableness of trustees' fees. . . . (Indeed, it is not obvious to me that anything more than a statement of the amount of trustees' fees paid over some relatively current period of time is necessary. For trusts recently established, the Code already requires disclosure of that information as a part of the periodic account.)

As a matter of clarification, it should be noted that the requirement that a number of items be disclosed in a periodic account is not limited to recently established trusts. See Prob. Code § 16062.

**§ 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, minimum fee, hourly rate, or transaction charge.

**Comment.** Section 15690 defines "trustee's fee" for the purposes procedure in this article governing increases in trustees' fees. This limited definition does not apply to provisions not in this article. The reference to "transaction charge" includes charges for deed preparation, stock sales, check writing, tax return preparation, and the like.

**Note.** The California Bankers Association (Exhibits p. 15-16) objects to the inclusion of transaction charges and hourly rates in this definition. CBA suggests that it is "inappropriate" since the "original concern expressed centered on minimum fees and ad valorem percentage fees."

CBA correctly characterizes the initial concerns that prompted this study, but the problems that prompted the study are not necessarily the only problems. In this particular case, the reason for including a broader description of fees is to provide a consistent approach. If fees are rising too much, the beneficiary probably does not care whether the fee is a minimum fee, hourly rate, transaction charge, percentage fee, or any other type. Including all types of fees in this definition also responds to the concern that a trustee may be tempted to make up a perceived "loss" in a percentage fee by relying more on hourly fees or transaction charges, should these fees be left uncontrolled.

It is difficult to understand CBA's objection to including hourly rates in this definition. An increase in hourly rates could have a substantial impact. The objection to including transaction charges is more understandable, since the need to charge such fees may not be within the control of the trustee, such as when new tax reports are required. But the staff has no reason to believe that all or even most transaction fees are simply reimbursements for expenses imposed by government. However, in recognition of the possibility that an increase in transaction charges may reflect duties imposed from outside the trust, Section 15691(b) has been drafted to exempt transaction charges of less than 10% per year.

**§ 15691. Application of article**

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

(b) The requirement of subdivision (a) does not apply to an increase in a transaction charge that is less than 10 percent per year.

**Comment.** Subdivision (a) of 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 15698.

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

Subdivision (b) makes clear that *de minimis* transaction charge increases are not subject to the procedure of this article or to court approval.

**Note.** *The California Bankers Association (Exhibits p. 15-16) is not satisfied with the de minimis provision in subdivision (b) since CBA objects to the inclusion of hourly rates and transaction fees in any way, as discussed in the note following Section 15690. CBA does like the de minimis concept, however, and would apply it to percentage and minimum fees so as to permit an increase of 10% per year without triggering the proposed procedure for notice and the opportunity to object:*

*Such an increase tied to a relatively small percentage change would allow trustees to receive increases to their fees in recognition of ongoing inflationary trends and costly increased regulatory and compliance requirements. In addition, a trustee would be entitled to increase its fees on a cumulative basis and not lose the de minimis increase amount provided in the statute by not increasing fees in any one year. The following is suggested:*

*"(b) The requirement of subdivision (a) does not apply to any increase in a trustee's fee that is no greater than 10% per year, calculated on a cumulative basis."*

*The staff has several observations on this proposal. First, 10% per year does not seem to be a "de minimis increase" when applied to the overall compensation for administering a trust. We had always assumed that percentage fees calculated on the value of trust property were beneficial because the trustee was rewarded for sound administration of the trust resulting in appreciating assets. It should also provide a hedge against inflation, since appreciation of trust assets should bear some relation to the rate of inflation. Hence, even without doing anything, the dollar amount of the trustee's fee will continue to increase in times of inflation. A flat fee, like a set transaction fee is a different thing, thus justifying a de minimis exemption.*

We are not clear on how the CBA proposal would work in the case of an increase in percentage rates. Could the trustee increase the ad valorem rate from, say, 1.5% to 1.65% under this proposal and then take whatever fee in dollars the increase generated without needing to follow the notice procedure? Or would the trustee be limited to a 10% increase in dollar amount, even though the percentage increase would yield a higher figure?

The staff is uncertain how this would affect the natural increase in the dollar amount of ad valorem fees resulting from appreciation of trust assets. If the fee is not increased, but trust property appreciates 12%, would the trustee be entitled to the whole fee, or only 83% of it? The situation is more confusing where assets appreciate and the trustee also raises a percentage and/or minimum fee. Would the fee stay raised, but be limited in application? Is the part of the increase in dollar amount that is due to appreciation lumped in with the part due to minimum fee or rate changes?

Finally, we are puzzled about the suggestion that "a trustee would be entitled to increase its fees on a cumulative basis and not lose the de minimis increase amount provided in the statute by not increasing fees in any one year." Does this mean that the trustee would be on a layaway plan permitting stockpiling of unused 10% cumulative fee increases? If so, the proposal is completely unacceptable. It would make the statute useless. After 7 or 8 years, a trustee who had not bothered to increase its compensation at the compounded 10% rate could double the rates and use the 10% chits put away in past years.

Having listed a number of problems, it is still possible that a useful policy could be pulled from this suggestion, assuming that the rate is set much lower than 10% and that permissible de minimis increases cannot be stockpiled. Some clarifications would have to be made in how the de minimis standard would apply in the case of ad valorem rate increases and appreciation.

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

15692. (a) Except as provided in Section 15691, if a trustee proposes to increase the trustee's fee, as to each trust that would be affected by the proposed fee increase, 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 or to receive a distribution of principal if the trust were terminated when notice is given. If a beneficiary is a minor for whom no guardian has been appointed, notice of the proposed fee increase shall be given to the parent having legal custody of the minor beneficiary and the parent may thereafter represent the interests of the minor beneficiary under this article.

(b) 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.

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 in part from Section 15640 (acceptance of trustee's resignation), with the addition of special rules concerning certain minor beneficiaries. 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).

§ 15693. Contents of notice of proposed fee increase

15693. Notice of the proposed increase of the trustee's fee shall include the following information:

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

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

(c) 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.

(d) 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.

(e) 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.

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

(g) 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.

(h) 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.

(1) A statement that if all the beneficiaries who are entitled to notice of the proposed fee increase agree in writing, the trustee may resign pursuant to Section 15697 or the beneficiaries may replace the trustee with a successor trustee pursuant to Section 15698.

**Comment.** Section 15693 sets out the required contents of a notice of proposed fee increase given under Section 15692. As to the liability for costs and attorney's fees, see Section 15696.

#### § 15694. Increased fee allowed if no objection

15694. 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 15694 describes two actions 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).

**Note.** *The California Bankers Association (Exhibits pp. 14-15) objects to giving "one beneficiary the ability to block a fee increase and force either a petition to the court or a resignation of the trustee." At the outset it should be noted that the situation is not as dire as suggested. The trustee is not limited to petitioning for the fee increase or for approval of resignation. The trustee may also drop the proposed fee increase, may seek a compromise, or may seek a different fee increase.*

*The issue of who should be able to extrajudicially forestall a proposed fee increase has been the most controversial matter in this proposal. CBA characterizes the proposed right as interference "with the proper administration of the trust by creating an unreasonable burden on the trustee to file" a petition to approve increased fees. The point was made at past meetings that the trustee is in the best position to file the petition. In addition, the potential liability for costs and attorney's fees chargeable against the objector and his or her interest in the trust should act as a significant brake on frivolous objections.*

*From a different perspective, it might well be asked why trustees should be permitted to increase fees in any event without a court order. Perhaps the statute is overly generous. The law was not clear on this point several years ago. Support for the existing power of the*

trustee to unilaterally charge a "reasonable" fee is not unanimous. A number of persons who responded to our 1987 questionnaire on this topic suggested (some of them vehemently) that fees should be increased only with court approval and that California should impose supervised administration on trusts in the manner of testamentary trusts in years past. In this light, expecting the trustee to petition to overcome a beneficiary's objection should not seem so burdensome. This placement of the burden of petitioning seems perfectly fair to the staff, particularly in view of the liability for costs and attorney's fees, and considering the relative positions and general sophistication of the parties.

The staff believes that the real bone of contention here is the one objector standard. It may seem unfair not only from the trustee's perspective, but also from the perspective of the other beneficiaries. Another reasonable approach is to require a greater representation of the interests of the beneficiaries in the objection process. CBA writes:

The CBA continues to believe that all beneficiaries should object to a proposed fee increase in order to trigger the new and dramatic rights given to beneficiaries under the statute. However, in order to suggest a workable and equitable solution, we propose as a compromise that more than 50% of both categories of beneficiaries, as that term is defined in Section 15692(a) of the proposal, must object. The statute would then provide that more than 50% of those beneficiaries "to whom income or principal is required or authorized in the trustee's discretion to be currently distributed" and more than 50% of those beneficiaries who would "receive distribution of principal if the trust were terminated when notice is given" must object in order to trigger the notice provision of the statute. We believe that this concept would be equitable to both categories of beneficiaries and would not favor one category over another, as is potentially the case in the current . . . proposal.

The staff believes that the suggested compromise is a reasonable one; requiring objections from dual majorities was seriously considered when the one objector rule was adopted for purposes of the tentative recommendation. Adopting a majority rule, requiring majorities of both present beneficiaries and remainder beneficiaries, would eliminate the argument that the lone objector is thwarting the wishes of the majority of beneficiaries and would also provide a stronger justification for putting the burden of petitioning on the trustee. Presumably the trustee would be more willing to seek a compromise or reconsider the fee increase when faced with opposition from the majority of both classes of beneficiaries, rather than just one beneficiary.

Accordingly, the staff proposes that a dual majority rule be adopted. The language suggested by CBA is appropriate, although we would use the word "majority" rather than the phrase "more than 50%."

#### **§ 15695. Procedure if beneficiary objects**

15695. 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 15695 provides for the trustee's options following a timely objection to the proposed fee increase. See Section 15697 (right to resign if all beneficiaries object). See also Section 15696 (liability for costs and attorney's fees).

**Note.** For a discussion of the comments of the California Bankers Association concerning this section, see the note following Section 15694.

#### **§ 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 15695, 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 in proceedings for approval of a proposed fee increase following receipt of a beneficiary's objection under this article. This section does not apply where the trustee seeks court approval of a fee increase initially by petition under Section 17200(b)(9).

#### **§ 15697. Resignation or removal if all beneficiaries object**

15697. (a) If all persons entitled to notice under Section 15692 object to the proposed fee increase in a writing delivered to the trustee within the time allowed, within 60 days after expiration of the time allowed for making an objection:

(1) The persons entitled to notice under Section 15692 may, acting together and without the need to obtain court approval, remove the existing trustee and select a successor trustee as provided in Section 15698. The trustee may not be removed under this paragraph if, before the expiration of the time allowed for making an objection, the trustee petitions the court for approval of the fee increase or withdraws the proposed fee increase by giving written notice of the withdrawal to the persons entitled to notice under Section 15692.

(2) The trustee may resign as trustee without the need to obtain court approval. The trustee's resignation under this paragraph is not effective until a successor trustee is selected.

(b) A trustee who resigns or is removed 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 15697 provides for the resignation or removal of the trustee if all the persons entitled to notice of a proposed fee increase object in writing within the time allowed. 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. See Section 15695 (procedure if not all beneficiaries object). Where a parent of a minor beneficiary is given notice pursuant to Section 15692, the parent may exercise the power to remove the trustee provided by this section. See Section 15692(a).

Note. Paul Gordon Hoffman of Los Angeles (Exhibits p. 7) opposes the right of the beneficiaries, acting unanimously, to replace the trustee following a proposed fee increase. He suggests that hostility between the beneficiaries and the trustee is not unusual and may be the natural outgrowth of implementing the settlor's intent. Mr. Hoffman would restrict the beneficiaries to a petition for court review of the proposed fee increase.

Russell G. Allen of Newport Beach (Exhibits p. 10) does not believe that all the beneficiaries should have the power to remove the trustee without petitioning the court. He suggests that it "effectively removes any check to protect the purpose or purposes of the trust relationship as contemplated by the settlor." The proposed section attempts to balance these interests by providing this right only in response to a proposed fee increase that is objected to by all of the beneficiaries. It is thus not a general right that can be invoked in other circumstances. Note as well that the right is not absolute; the trustee can avoid removal by withdrawing the proposed fee increase or petitioning the court for approval of the proposal. Thus, the trustee is not locked in, suffering under inadequate fees because of the threat of removal if it dared to propose a fee increase. The course is not locked in since the procedure provides several escape hatches and is intended to provide a balanced set of rights on all

sides. Consequently, if the trustee is interested in honoring the settlor's intent (and assuming the settlor would not object to the proposed fee increase), the trustee has to take some care in proposing the fee increase, in communicating to the beneficiaries, and in working out a compromise if there is significant opposition. Otherwise, the course is to petition the court for a fee increase before the right to remove the trustee vests. The staff believes that the concerns expressed by Mr. Allen are adequately answered by the proposed procedure.

Michael S. Whalen of Los Angeles (Exhibits pp. 12-13) identifies a procedural bug in this section. The problem arises because two counterpoised procedures are subject to the same time period. Thus, if the beneficiaries wait until the last moment during the "time allowed for making an objection" the trustee will not be able to petition the court for approval of the fee increase or withdraw the fee increase and thereby terminate the power of the beneficiaries to remove the trustee. Mr. Whalen writes:

I am concerned with avoiding a situation where one or more disgruntled beneficiaries could abuse this process by using the fee "dispute" as a pretext to oust a corporate or individual trustee imposing appropriate controls. It appears to me that the language now proposed would allow the objecting beneficiaries to wait until the last hour of the notice period provided under Section 15692 and deliver their objections to the trustee. By waiting until the last moment, the beneficiaries could effectively cut off the trustee's option to avoid removal under this new section. To avoid such a tactic, it would seem appropriate to provide the trustee some period of time following the expiration of the initial notice period in which to respond to the beneficiaries' timely objections, either by a petition to the court or by the withdrawal of its fee request.

Mr. Whalen suggests that this section be revised to provide a 10-day period after expiration of the time allowed for making an objection.

The staff agrees that this is a possible problem and suggests that the trustee be provided at least 15 days from receipt of the objection within which to act. Fifteen days is the same as the general period of notice under Probate Code Section 1220, and so seems an appropriate time period. The simplest way to remedy the problem is to add 15 days to the trustee's time to act, as suggested by Mr. Whalen, thereby providing a 75-day period for the trustee. The relevant sentence in subdivision (a)(1) would be revised as follows:

~~The trustee may not be removed under this paragraph if, before the expiration of the time allowed for making an objection~~ within 15 days after the expiration of the time allowed for making an objection, the trustee petitions for court approval of the fee increase or withdraws the proposed fee increase by giving written notice of the withdrawal to the persons entitled to notice under Section 15692.

An alternative would be to provide that the trustee must act in all cases within 15 days after receipt of the objection, regardless of

how much of the original 60-day (or longer) period has run. However, there does not seem to be any particular need to hurry this process along. A third alternative would be to make clear that the trustee has not less than 15 days to respond so that the 60-day (or longer) period is extended only if the objection is received sometime within the last 15 days of the period for making objections.

**§ 15698. Selection of successor trustee**

15698. If a trustee resigns or is removed pursuant to Section 15697, 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.

**Comment.** Section 15698 governs selection of a successor trustee to fill the vacancy created by resignation or removal of a trustee pursuant to Section 15697 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 § 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); *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).

*Note.* *Russell G. Allen of Newport Beach (Exhibits p. 10) opposes this section on the grounds that it is undesirable to give statutory recognition to exemplary damages against trustees for breach of trust. Mr. Allen considers the deletion of this provision from the trust bill in 1986 to be "the most beneficial change to the proposed law made during the course of the legislative process." We have discussed this point at past meetings. Traditionally there was no authority for awarding punitive damages against trustees. In recent years, however, the traditional doctrines have weakened, and several cases have awarded exemplary damages. See the text of this tentative recommendation, supra at 4. While the California cases did not face the doctrinal issues, the result is that exemplary damages have been awarded and presumably will continue to be. This has been the trend in recent decades. It is in this context that the treble damages limitation is proposed.*

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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 prior law and not a substantive change.

**Note.** Neil S. Bezaire of San Marino (Exhibits pp. 4-5) recommends adoption of a statutory fee schedule like that applicable to probate fees. In support of this proposal, Mr. Bezaire cites the reasons given by the Commission for keeping the percentage statutory fee in probate:

*A percentage fee takes into consideration the responsibility assumed, complexity of the matter, and enables the attorney*

to handle all trust matters even the small estates. The clients seem to prefer the certainty of the percentage arrangement rather than an open ended hourly rate. The percentage fee also encourages the trustee and the attorney to work quickly and efficiently rather than stringing it out on an hourly basis.

Of course, this makes some sense; courts have tended to rely on probate fee schedules as a benchmark in reviewing trustees' fees and the fee schedules of corporate trustees reflect this approach. But viewed another way, it can be said that we have the best of both worlds in trust law. We have had the statutory fee as an unofficial, general guideline and yet we also have freedom of contract, leavened by a standard of reasonableness. The staff sees no compelling reason to impose a statutory fee in trust administration.