Study L-640 7/17/84

Memorandum 84-58

Subject: Study L-640 - Trusts (Comments on Trust Memorandums)

In recent months we have received several letters commenting on the staff memorandums and draft statutes concerning trust law. Most of these letters have already been distributed, but the staff decided to collect and redistribute them for easier reference. Consequently, six letters are attached to this memorandum:

Exhibit 1: Executive Committee, Probate and Trust Law Section of Los Angeles County Bar Association, April 16, 1984. (The parts of this letter relating to nontrust matters have been omitted and the pages renumbered.)

Exhibit 2: Executive Committee, Estate Planning, Trust and Probate Law Section of State Bar, April 25, 1984. (The parts of this letter relating to nontrust matters have been omitted and the pages renumbered.)

Exhibit 3: Executive Committee, Probate and Trust Law Section of Los Angeles County Bar Association, June 8, 1984.

Exhibit 4: California Bankers Association, June 20, 1984.

Exhibit 5: Memorandum from Melvin H. Wilson on behalf of California Bankers Association, June 14, 1984.

Exhibit 6: Executive Committee, Estate Planning, Trust and Probate Law Section of State Bar, June 20, 1984.

These letters will be referred to in the supplementary memorandums that analyze comments on each subject. Letters that deal only with the subject matter of one memorandum will be attached to the supplement on that subject.

Respectfully submitted,

Stan G. Ulrich
Staff Counsel

EXHIBIT 1

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April 16, 1984

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

Re: April Meeting Agenda

Dear Commissioners:

On behalf of the members of the Executive Committee of the Probate and Trust Law Section of the Los Angeles County Bar Association, we submit our comments on various studies which are scheduled for discussion at your meeting on April 27 and 28, 1984. These comments do not reflect Supplements to Memoranda as they were not received in time for sufficient review by the whole committee before this letter was prepared.

. . . .

Study L-640 - Trusts (Scope of Study)

We assume that the decision to codify only essential elements of the law relating to express written trusts in the Probate Code is not a decision to repeal the provisions regarding constructive trusts and resulting trusts which remain in the Civil Code.

Study L-640 - Trusts (Formalities for Creating Trusts)

Subsection (e) of the unnumbered statute "Methods of creating a trust" should be modified to read, "An enforceable promise. . . ."

We concur that trusts should be created by a writing.

We also concur in explicitly adopting the rule, "Consideration is not required for the creation of a trust." We also agree with the deletion of the requirement of trustee acceptance in order to have a valid trust.

Study L-640 - Trusts (Presumption of Revocability)

We strongly believe we should keep the statutory presumption of revocability found in Civil Code Section 2280. California purposely changed from the common law because of horror stories that were numerous. Well-drafted trusts contain explicit statements of revocability or irrevocability, as the case may be. However, we can't count on all trusts being well-drafted nor can we count on all trustors to carefully read the instrument. The evidence to the contrary is overwhelming. Many trusts are drafted by trustors themselves, perhaps utilizing form books that do not address the issues raised by California law. We should preserve the ability of such trustors to correct their mistakes. Since most trusts currently drafted are revocable trusts, a presumption that favors the majority is not unreasonable. The California rule was enacted as consumer protection and should be retained as such.

The staff has pointed out a problem of application of the California rule in a multi-state context which should be addressed. The appropriate solution to the problem is not to change California's general rule, but to create a separate rule for a trust created outside California which becomes subject to California law due to its administration here. The rule could simply state that whether the trust is presumed revocable or irrevocable shall be governed by the law of the state in which the trust was created, unless otherwise provided in the trust instrument.

Study L-640 - Trusts (Indefinite Beneficiaries and Purposes)

The current rules on indefinite beneficiaries and indefinite purposes are a rare triumph of rigidity and technicality over the usual policy of assuring that the testator/trustor's wishes are fulfilled. To hold that a power which would be valid if expressed as a power becomes invalid merely because the word "trust" appears is ludicrous. While there are situations in which the testator/trustor's intent cannot be ascertained, in many others, the intent is perfectly clear, even if some of the details are not specified. If the testator/trustor trusts the executor/trustee to select beneficiaries or trust purposes, why should the courts refuse to permit the executor/trustee to exercise this discretion?

We support the codification of the rule which would validate a trust if (1) a definite beneficiary or beneficiary class is designated, (2) a class is sufficiently described so that it can reasonably be determined that a person is within it, and (3) the trust gives the trustee or another person the power to select the beneficiaries.

We also support validating trusts for "indefinite purposes" to carry out the intent of the trustor through codification of Sections 123 and 398 of the Restatement (Second) of Trusts.

Study L-640 - Trusts (Trustee's Duties)

In general, the proposed legislation is an improvement on the current law in the sense that it consolidates many provisions found in differing locations and puts them in a logical order in one location. One of the trustee's duties found in the Restatement (Second) of Trusts which we did not notice in the proposed legislation is the duty not to delegate to others the doing of acts which the trustee can reasonably be required to personally perform. It may be that this is more appropriately discussed under the exercise of discretionary power, a duty commonly believed to be non-delegable. However, it should be included somewhere. Other duties that perhaps should be listed are the duties (1) to keep trust properties segregated, (2) to make trust property productive, (3) to deal impartially with beneficiaries where there are multiple beneficiaries of one trust, and (4) duties of co-trustees with respect to their joint administration of the trust.

There are some problems to Section 4321 which establishes different standards of care for different trustees. To date, only minimal guidance has been given to the court in determining which trustees should be held to a higher standard and how much higher the standard for each should be. It is not so much a problem for corporate fiduciaries, to whom this rule is generally applied anyway. But what about individuals who may have some "greater skill"? What standard should be applied to an attorney acting as fiduciary? What about an attorney who is not a trust specialist? What about an accountant? Is he to be held to a higher standard? How much higher? Is there to be a higher standard for a businessman than a housewife? What if the trustor thought that the trustee had "special skills," but the trustor misperceived the existence of those skills?

Study L-640 - Trusts (Trustees' Powers)

We support an automatic power statute on the grounds that it gives needed flexibility to trustees in administering trusts and reduces the costs to trusts, trust beneficiaries and the general public by eliminating the need for many petitions to the courts for needed additional powers. For these reasons, we also support application of this rule to trusts already in existence.

The staff is concerned about "the parade of horribles that might otherwise issue from the uncontrolled exercise of trustees' powers." We are talking about an automatic grant of powers; we are not talking about the controlled or uncontrolled exercise of those powers. Trustees' powers would be subject to the same controls as presently exist, regardless of whether those powers are conferred in the trust instrument, by the court upon petition, or by automatic statutory grant. Remedies for abuse of discretion or misuse of power are not lacking.

With regard to the specific powers, Professor Haskell's concerns over proposed Sections 4422 and 4432 appear to be misplaced. He seems to feel that a bank serving as trustee should not be able to retain bank stock in a trust or to keep trust funds on deposit in its own bank. It would be rare that a corporate trustee would purchase its own shares. What an invitation to a surcharge if there is any loss at all! Thus, we are talking only of retaining inception assets, and that is precisely what most trustors desire. Corporate trustees have had a great deal of difficulty in explaining to trustors and beneficiaries why at least a portion of a large block of their own stock (which may be a blue chip holding) should be sold and the proceeds used to diversify the portfolio.

We see little problem with permitting a corporate trustee to keep funds on deposit in its own bank. It is more convenient, efficient and economical, particularly with internal computer systems which permit unlimited transactions and instant access to funds. Of course, the rates must be competitive. For Bank of America to use Bank of America when Crocker is paying significantly higher is again an invitation to a surcharge action. If the rates are comparable, however, it hardly makes sense to require that a Bank of America trust officer walk the three blocks to Crocker and wait in line each time a deposit or withdrawal is necessary. Neither should Professor Haskell like the idea of handling all transactions by mail, with the attendant loss of use of funds. We doubt that major corporate fiduciaries are going to risk a surcharge action, with the unfavorable publicity which might result, just to make a few dollars off a deposit account. Further, use of deposit accounts by major corporate fiduciaires is not all that common these days anyway. Most use some kind of Cash Fund, a commingled fund permitting unlimited daily deposits and withdrawals and paying more than money market accounts. Beneficiaries seem quite happy with this vehicle.

We suggest more detail be added to proposed Section 4474 so that payments can be for the "benefit of" a disabled beneficiary as well as "use of." Also payments to a non-relative as Custodian under the Uniform Gifts (or Transfers) to Minors Act should be included.

We object to portions of proposed Section 4478. It has long been the general rule that trustees may delegate administrative duties but not discretionary duties. This is especially true with regard to discretions which are "sole, absolute or uncontrolled." We believe that rule should be continued and subsection (c) removed. Furthermore, we are somewhat concerned with how subsection (b) relates to the trustees' general duties of care. Perhaps careful investigation of the agents prior to hiring should entitle the trustee to rely on their advice once they are hired. On the other hand, there should be some periodic

assessment of performance. Just how these two concerns interrelate and how much to try to regulate by statute is a concern of our committee.

We concur that there is no need to enact UTPA Section 3(b).

Study L-640 - Foreign Trustees.

As anyone who has tried to draft a trust using one corporate trustee and having assets which consist of real property in more than one state has discovered, the difficulties are real. Even though real property held by trusts is considered to be a personal property interest in many states, in those states where it is not, the necessity for a local trustee becomes apparent. A reciprocity scheme would be advantageous to expand the role of the California corporate trustees out of the state. Given the standing of California financial institutions in the nation as a whole, we think it's more likely that a reciprocity scheme would benefit California institutions than that it would benefit foreign corporate trustees. At the same time, such a scheme would benefit many donors and testators when designing trusts. Furthermore, such a provision may actually facilitate the changing of situs of trusts from one state to another and the transfer of jurisdiction for supervision of those trusts. Anything that would make that process easier would be appreciated by local beneficiaries of trusts established by a person in a generation one or two generations removed who may have lived in another state.

Despite our preference for reciprocity, it seems that most any of these options are acceptable. Whatever is done, we suggest more analysis. While it is true that some states permit some foreign corporations to act, our research has revealed no state which permits all foreign fiduciairies to serve as trustee. While there are a few states which will permit a national bank with its principal office in California to take a few limited actions with regard to assets located in those states, we have found no state which will allow such a bank to truly serve as trustee.

The whole question of interstate banking is receiving a great deal of scrutiny from the banking industry. Different segments of a bank may prefer different alternatives. For example, the trust departments of some banks favor limited reciprocity with some other states, while the commercial departments of the same banks may oppose any expansion of the powers of an out-of-state bank. Others may favor permitting an out-of-state fiduciary to take limited actions as long as it does not regularly conduct business here.

We should be reluctant to make any sudden changes to the present system. While there are trusts with out-of-state real property, title to which cannot be held by a California corporate fiduciary, there are several ways to handle the situa-

tion, including the appointment of an ancillary trustee in the other state. This procedure is neither so cumbersome nor so expensive that it warrants an abrupt shift in approach, particularly since there does not yet appear to be any consensus with regard to a desirable alternative. Further study and some input from the banking industry might be helpful.

Study L-640 - Transfer of Trust To or From California

These provisions appear to be sound changes. However, we question the retention in proposed Section 4653(h) of the requirement that the petition state "whether there is any pending civil action in this state against the trustee." This requirement should be limited to natural persons, as the staff has recommended with regard to the requirement in proposed Section 4653(d) that the petition give the age of the trustee "if the trustee is a natural person." We are not aware of any corporate fiduciary in California that does not have civil actions pending against it, and the fact that there are such actions is certainly not news to the judge who may hear a petition to transfer a trust.

Study L-640 - Revised Uniform Principal and Income Act

First, we agree with the staff that Section 4801 should be omitted. It should be clear at this point in time that principal and income as defined for probate and trust accounting purposes does not relate to the calculation of income for tax purposes, and we can think of no other reason for such a section being in the law.

Moving these provisions to the Probate Code from the Civil Code appears to be desirable. It also appears to be desirable that if the prudent man standard is removed from the ordinary trust provisions regarding trustees, it should also be removed from the principal and income act.

We hope to be able to give additional written input to the process prior to your meeting.

Very truly yours,

Valerie J. Merritt

VJM:rhy/170

EXHIBIT 2

ESTATE PLANNING, TRUST AND PROBATE LAW SECTION
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April 25, 1984

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
4000 Middlefield Road, Suite D-2
Palo Alto, California 94306

Dear Mr. DeMoully:

The Executive Committee of the Estate Planning, Trust and Probate Law Section submits the following comments on selected LRC memoranda to be discussed at the April 27-28 meeting of the Law Revision Commission. We will supplement this report as the members of our section are able to complete their studies of additional memoranda.

For your information, the Executive Committee governs a section of approximately 4,000 lawyers from throughout California. The Executive Committee and its Advisors consist of judges and lawyers from widely dispersed geographical areas of California, who represent clients of diverse cultural, ethnic and economic backgrounds, and who are associated with large firms and small, and public practices and private.

. . . .

Study L-640 - Trusts

Presumption of Revocability - Memorandum 84-18

We are opposed to changing the presumption of revocability. Such a change poses a trap for the unwary. Allowing a trust to be revoked rarely does any damage. Preventing revocation can cause irreparable damage. A decision to preclude revocation should be an affirmative one.

Indefinite Beneficiaries and Purposes - Memorandum 84-19

We support the proposal. The proposal would establish a policy that if the trustor's intent can be ascertained, it should be carried out. The policy issue is much like that of favoring testacy over intestacy.

Trustee's Duties - Memorandum 84-21

We do not like the suggestion that the language of Texas Trust Code, Section 113.051 be adopted, because the language is too general to be of much help. We are also concerned about future arguments being made that Texas law should be considered (or perhaps controlling) in cases involving questions concerning Trustees' duties. We are concerned about the reference in the Texas Trust Code section to the "common law." If the section were adopted, the reference should be to the duties imposed on Trustees by the case law of California rather than the "common law." If something new has to be done, we would be in favor of approving the first two pages of Exhibit 1 to the Memorandum (with the exception noted below). However, we concurred in the general comment (which applies not only to Memorandum 84-21 but also to all amendments in the Trust area which may be under consideration) that unless a substantive change is being made by language it is preferable to leave current sections and current language in place without amendment.

There was one exception to the general approval of the suggested language on pages 1 and 2 of Exhibit 1 to the memorandum. We believe that the last sentence of proposed Section 4304(b) should be changed so that notice is required.

Concerning the "Standard of Care," we do not have any substantive objections to the discussion and proposals in the memorandum but, again, unless changes in language are meant to have substantive significance it is usually better to retain the existing language. We approve of Section 4320(b) on Exhibit 1 which provides that individual investments are to be considered as a part of overall investment strategy.

As to "Trustee's Duty to Inform and Account to Beneficiaries," it should be possible to waive trust accountings in all circumstances, whereas the comment to Section 4341 in Exhibit 1 implies that the accounting required on termination or change of Trustees could not be waived. Whatever requirements as to the providing of accounting and other information are eventually adopted, such requirements should not be inconsistent with or cause unnecessary additions to the information required by Probate Code Section 1120.1a. Further, it should be remembered that those requirements are imposed only on corporate trustees of trusts no longer subject to continued court supervision.

While furnishing a copy of the income tax returns may fulfill a general duty to account, there should be a specific provision allowing the beneficiary to demand and receive a detailed accounting at least annually. The income tax returns are informative, but not detailed, and may not disclose tax-exempt income or non-deductible expenses.

The current language in Civil Code, Section 2261(4) regarding deviations from the terms of the Trust does not seem to be retained. That provision should be retained.

Trustee's Powers - Memorandum 84-22

We are opposed to the proposal to grant statutory powers to all trustees. We believe Trustors who draft their own trusts are not likely to exclude objectionable powers. Certain specific powers present particular problems. For example, §§4420 and 4430 should be coordinated with the prudent man rule legislation. Section 4422 (power to hold property) could present a tax problem for a marital deduction trust if the trustee receives unproductive property. Section 4426 (which allows entering into a new business) strikes us as an inappropriate automatic power. It is common to exclude such power from trusts involving corporate trustees. Section 4428 seems unnecessary, and may be construed to be a limitation rather than a power. Section 4464 should state that borrowing is for a trust purpose. Section 4478 (hiring persons) is too broad, especially to be an automatic power.

Revised Uniform Principal and Income Act - Memorandum 84-32

The above memorandum reviews the Revised Uniform Principal and Income Act as it has been enacted in California, and suggests possible new variations. It should be remembered that this Act provides for rules of construction regarding principal and income of trusts. Accordingly, we are not commenting upon several of the topics discussed in the memorandum because we believe that the present law is adequate for most general purposes.

The California version of the Act is now set forth in Civil Code Sections 730-730.17, but will be moved appropriately to the Probate Code and renumbered as suggested sections 4800 through 4817.

Also because these are rules of construction, we suggest that Section 4816, (which explicitly states that "Except as specifically provided in the trust instrument or the will or in this part, this part applies to any receipt

or expense ...") should be renumbered and placed at the beginning of the Act.

We would prefer retaining the definition of "trustee" in the definitional section 4802, rather than having it cross-referenced to Probate Code Section 84. This is for convenience sake.

We believe that Section 4803(a)(3) should be changed as per the staff recommendation so that there is consistency in following the prudent investor standard contained in Civil Code Section 2261 and proposed to be changed by AB 630; this can be by cross-reference. We prefer the Nebraska variation of 4803(b), that no inference arises "that the trustee has improperly exercised such discretion from the fact that the trustee has made an allocation contrary" to the Act.

We recommend retention of the California variation of the Act in Section 4805 regarding apportionment of income. California's variation is probably based upon administrative simplicity and does not require day to day allocation of rents, annuities, and interest on bank and savings and loan association accounts.

California retains the "no amortization" of discounted bonds, but the staff has recommended deletion of this rule, apparently trusting to drafters the ease of changing the rule if desired. We would not rely upon draftsmanship, and believe that existing law is better for a general rule of construction.

We would prefer to reverse the "no carry-over" rule for income losses of business and farming operations in Section 4809. In other words, losses should be carried over from one year to the next. There are two primary reasons for reversing the present rule.

First, the typical trust in California is created for estate tax purposes, or to prevent a guardianship for minors. For minors, the income may be accumulated or distributed during minority, but when the trust terminates upon the child attaining a given age, the principal is distributed to the child. In other words, the income beneficiary and the remainderman is the same person. The estate tax trust is generally designed to avoid having the trust principal taxed in the income beneficiary's estate. One spouse places his or her property in trust. The other spouse is the income beneficiary and normally has a right to invade trust principal for health and reasonable support. The goal is to preserve principal (so it will not be taxed in the beneficiary spouse's estate). The present rule of allocating losses to principal conflicts with that goal, without giving any additional benefit to the income beneficiary who can already invade principal.

The second primary reason for reversing the present rule is based on present commercial considerations. Farmers expect loss years. It is the average over several years which they try to achieve. Allowing losses to be carried over is a realistic recognition of the nature of farming. Furthermore, farmers frequently pre-sell crops; pre-pay rent; carry over crops unsold from one year to the next to obtain better markets; pre-pay expenses for fertilizer or land preparation; and defer payments on crops sold through co-ops or packing houses. All of these can distort income from one year to the next. Only by establishing a rule for carrying over trust losses from one year to the next will the income beneficiary receive the true business income.

We believe the trustee's "absolute discretion" to determine income and principal from natural resources, timber and other property subject to depletion ought to be retained, including the trustee's absolute discretion to determine whether to allocate up to 27 1/2% of gross receipts to principal as a depletion allowance in Section 4810. The staff recommended possibly changing the latter percentage to make it more general, to be consistent with existing federal tax laws. Apparently the 27 1/2 figure was the historically used figure, but it can be changed if necessary in the drafting instrument.

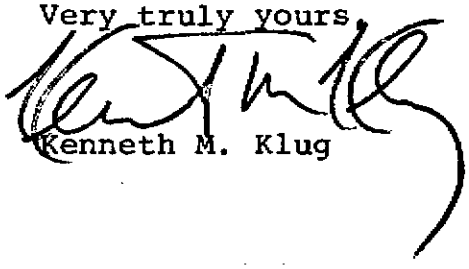
We concur with the staff recommendations and see no reason to treat income receipts from timber different than income from other natural resources; this is in line with the Oregon version of the Act. However, timber on the property at the time the trust is established should be deemed principal. Consideration should be given to developing some means of segregating income from principal without the necessity of an appraisal at the time the trust is established. Perhaps a formula approach based on average harvest age for the type of tree cut could be developed. Allocating all timber to principal with a factor for unproductive property would be reasonable.

California presently permits 5% of unproductive property to be attributed to delayed income. For a general rule of construction, this still seems satisfactory, although the staff is concerned with the percentage being somewhat low under present economic conditions. We recommend that the Commission bear in mind that farmland has historically produced a low rate of return. Increasing the percentage of deemed income from unproductive property would have a major impact on trusts which own farm property.

Finally, California's version of Section 4814 permits flexibility in the trustee by providing an absolute discretion to determine principal and income allocation of charges, whereas the Act is specific. We see no reason to change California's version.

As a general comment relating to the Commission's work on the trust law, I should reiterate that we would prefer to retain existing language where no substantive change is contemplated. Where California courts have already decided cases based on existing language, lawyers have drafted documents in reliance on those cases. It would be unfortunate to depart from the existing language (and judicial interpretation) if no change in substance is intended. The people of California should not be required to incur the expense of overhauling their trust documents to fit within new concepts, and lawyers and trustees (especially corporate trustees) should not be forced to initiate contact with all former clients and trustors to warn them of changes which may affect existing trusts.

Very truly yours,



Kenneth M. Klug

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EXHIBIT 3

Memorandum 84-58

Study L-640

June 8, 1984

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

Dear Commissioners:

On behalf of the members of Executive Committee of the Probate and Trust Law Section of the Los Angeles County Bar Association, we submit our comments on various studies which are scheduled for discussion at your meeting on June 21 through 23, 1984. We would like to draw your attention to the fact that a number of studies which we made comment on in our letter dated April 16, 1984, were not discussed at your meeting of April 27 and 28, 1984. Therefore, these discussions are supplemental to the prior ones and the prior ones should also be considered at your meeting in June.

When we received our report from Valerie J. Merritt, Secretary-Treasurer of our Section, as to the April meeting, we were concerned that matters were discussed on the agenda which had been received so late there was not sufficient time for our committee to comment upon them, but other memoranda which we received in February and commented upon were not discussed. While we can understand the need for discussing memoranda which directly affect pending legislation early in your session, we do not understand why memoranda regarding pending studies which are not yet to the stage of proposed legislation shouldn't be discussed in the order in which they are produced. That way meaningful, thoughtful and complete discussion can be had about memoranda where there was time for sufficient commentary to be gathered from the State Bar, local bars, or even the commissioners themselves.

We note with approval the fact that on the proposed agenda dated May 10, 1984, the two-day discussion on trusts will begin with those topics submitted prior to the April meeting, with new memoranda deferred to the end of the meeting. We believe that that would be the best practice for all agendas. On the other hand, we also note that certain issues of probate law and procedure are scheduled to be discussed at the commencement of the meeting and cover memoranda which were not received by our members, and presumably not by others, until June 5 (as to some) or later (as to others still not received).

Trustee's Duties -- Memorandum 84-21, Study L640

We would like to reiterate all of our suggestions found in our letter to the Commission on April 16, 1984. Furthermore, having seen the commentary to the Commission by the Estate Planning, Trust and Probate Law Section of the State Bar of California (hereafter "State Bar Section"), we would agree that any reference in the Code to "common law" should be deleted and should instead refer to the "case law of California," so as to make it clear that we are not dealing necessarily with the general common law but more particularly with the case law as it has evolved in our own state.

We would like to suggest an additional change to subsection (d) of Section 4341. We believe that a beneficiary should have the right to waive any accounting, not just annual accountings. Therefore, we believe Section (d) should be changed to read:

> "The trustee is not required to furnish an accounting (whether annual, at the termination of the trust or upon a change of trustees) or income tax returns to any beneficiary who has waived the right to such accountings in writing. Any waiver of rights under this Section shall specify whether it includes annual accountings, accountings upon change of trustees, accountings upon the termination of a trust or all of the foregoing. A waiver of rights under this section may be withdrawn in writing at any time and has no effect on the beneficiary's right to request information pursuant to Section 4340."

Finally, we suggest that section (f) be added to the statute to indicate that the trust instrument has the power to vary the duties of the trustee, including the duty to account. If it is not done in a new subsection (f), then the lead-in to subparagraph (a) should state "Unless the trust instrument otherwise provides, at least annually . . . ."

While many people seem to believe that a copy of the fiduciary income tax returns of the trust is a substitute for an annual accounting, we do not believe it is entirely adequate. There are many items of information to a beneficiary which may not be reflected on income tax returns. These would typically

include income from assets which do not generate taxable income and the value of investments which are not sold or exchanged. They may also include payments of non-deductible expenses or payments to related parties. At the minimum, in addition to the income tax return, a trustee should prepare annually a statement of the assets on hand at the end of the accounting period and some reflection of whether the value of those assets has increased or decreased from its carry value. It may be better still not to allow a fiduciary income tax return to substitute as an account.

We also concur with the comment of the State Bar Section stating that the current language in Civil Code Section 2261(4) should be retained. We suggest that it be added to Section 4303. Located there, it would make it clear that the duty to obey the trust is not absolute. Deviations from the terms of the trust may be authorized by the court in certain circumstances.

Trustee's Powers - Memorandum 84-22, Study L640

Once again we refer you to our letter dated April 16, 1984. We would like to especially reiterate our objections to proposed Section 4478. In addition, subdivision (a) should be modified by omitting "administrative" and substituting for it "his or her".

We do not believe that alteration of Section 4422 is the solution to improperly drafted marital deduction trusts. We believe that marital deduction trusts should be specially dealt with in the drafting of the instrument or in special legislation that allows reformation of marital deduction trusts. If a trust which is not a marital deduction trust received unproductive property, the trustee should be allowed to hold that property if it otherwise appears to be an appropriate investment given the intent of the trustor as expressed in the document or the investment strategy generally.

We have noted the comments of the State Bar Section regarding proposed Section 4426. While we believe that the continuation of participation in the operation of any business enterprise is important when a trustee receives business entities at the inception of a trust, and while we also believe that the ability to change the form or organization of such a business or enterprise is important to the trustee (particularly when the change in form may limit the liability of the trust), we share the concern of the State Bar about allowing trustees to enter new businesses as an automatic power. We believe that the language of Section 4426 should be tightened to make it clear that the

trustee may continue to participate in the operation of any business or other enterprise received by the trustee at the inception of the trust or by transfer from the donor to the trust. We do not believe that the trustee should be allowed to enter into new business holdings without prior court authorization.

We also agree with the State Bar Section that Section 4464 should be amended to read "The trustee may borrow money for any trust purpose to be repaid from trust property or otherwise."

Breach of Trust - Memorandum 84-23; Study L640

This was one of the memoranda received too late for inclusion in our commentary dated April 16, 1984.

One problem with trying to codify the rules in this area is that to be too specific is to be too rigid. As in our comments earlier, we believe that the new statute should not make reference to the "common law," but rather to "California case law."

The language with regard to the statement of remedies is in general fine, except that we have a few technical comments. In subsection (3) of subsection (b) on page 10 of the memo, the beneficiary is filing an action "To compel the trustee to . . . surcharging the trustee." Obviously the trustee does not surcharge the trustee. Only the courts can surcharge a trustee. Grammatically that particular subsection does not make sense. Another comment on language is that subsection (8) refers to a lien or constructive trust "of" trust property. It should be a lien "on" trust property.

With regard to the measure of damages, we believe that California should adopt the language of the Restatement Sections 205 and 204. We believe that it may be a good idea to codify the essence of comment (g) to Restatement Section 205. Perhaps such a codification could read: "Notwithstanding the foregoing, the court may excuse a trustee from damages for a breach of trust in whole or in part where the trustee has acted honestly, in good faith and reasonably and ought fairly to be excused."

Since the codification of rules tends to automatically include the suggestion that perhaps the law is being changed, perhaps the statute should include liability for attorneys' fees incurred by the beneficiary in proceedings involving breach of trust. They are currently allowed if the beneficiary's actions have resulted in common benefit to the beneficiaries as a whole,

a group of them, or the trust estate. The common benefit or common fund theory of attorneys' fees may perhaps advisably be codified. If the trust estate is liable, perhaps also the Court should be authorized to award attorneys' fees to beneficiaires from the trustee.

In general, we approve of the codification of Section 207 of the Restatement. However, we believe that the "such other rate as the court . . . may determine" portion of subsection (1) should be limited so that it is either the legal rate or "the interest actually received by the trustee or which the trustee should have received." Subsection (2) on the compounding of interest is generally sound. Our reasons for concern about subsection (1) are that the legal rates should be a floor to the interest rate and "other rates" should not be higher unless the circumstances are such that the trustee actually did receive higher amounts of interest or should have received higher amounts given the circumstances at the time.

We have concern about codifying Restatement Section 224 regarding the liability of a trustee for breach of trust by a co-trustee. Specifically, we are concerned about subsection (e) of subsection (2). Just how far must a co-trustee go "to compel a co-trustee to redress a breach of trust?" Is the non-breaching trustee obliged to file suit against his co-trustee? Is he supposed to independently determine whether an act by his co-trustee constitutes a breach? Can the non-breaching trustee wait until the court determines that a breach has occurred? We believe that perhaps that particular subsection should be dropped. We are reluctant to see a co-trustee's liability for the acts of his co-trustee increase too greatly in situations where there was no affirmative consent to or participation in the acts later determined to be improper.

The whole issue of the liability of co-trustees for the acts of the other is also tied in to duties of the trustees and the issue of proper delegation. It should be noted that participation or improper delegation or failure to exercise care are all elements for a liability of breach of trust of one trustee being attributed to the other. All of these areas cause special concern in the case where one co-trustee has or appears to have more expertise than the other. For instance, decedent has named his widow and his investment adviser as co-trustees. Decedent probably expected his widow to rely upon the advice of his investment adviser in deciding upon the investments of the trust. May the remaindermen (perhaps children of decedent's prior marriage) sue the widow for improperly delegating investment

decisions to the investment adviser? While it will be up the court to determine whether the widow's delegation to the investment advisor was "improper," we should be careful to keep these types of situations in mind when we are drafting legislation applicable to all. We would not want to unduly limit the court's discretion.

We are not quite sure what rule the staff is proposing for the statute of limitations and discharge by court decree. In the case where an accounting has been made to a court which fully discloses the matter in question, then we believe that the six months period allowed under C.C.P. § 473 is sufficient. A beneficiary with notice of the formal hearing has an adequate chance to request continuances and have the matter fully heard well before any order is entered. Once an order is entered, it should be final within the same six month's period of any other judgment.

If the accounting did not fully disclose the subject in question, the staff appears to propose a time period of one year from the discovery of "the facts" or from the time when the beneficiary should have discovered them. There is then an ambiguous reference to the general statute of limitations but not the four-year statute. We assume that this reference is to the three-year statute of limitations for "fraud." If that is so, there seems to be a conflict between the staff's proposal of one year from discovery of the underlying facts and the general statute of limitations' application of a three-year time period from discovery of the facts. One or the other ought to apply.

We read Civil Code Section 2258 as giving a fairly broad mandate to the trustee to follow all the directions of the trustor, including those which may be contrary to the usual rules of trust law. Furthermore, Section 222 of the Restatement is an appropriate recognition of the fact that a trust instrument can relieve the trustee from liability for certain types of breach of trust. In most situations where the trust instrument explicitedly relieves the trustee from liability for certain types of breach of trust, the trustor is dealing with the case where one beneficiary may suffer but others may gain or the trustor has envisioned that all beneficiaries might suffer in the short term so as to create long term benefits. A common example of the former is where the trustor explicitly authorizes the trustee to favor the surviving spouse over remainder beneficiaries, even though that violates usual trust principles of "fairness."

Examples of the latter may include provisions requiring a trustee to hold certain closely held businesses in trust, and exculpating the trustee from paying dividends from those businesses if the trustee determines that the interests of the business require an infusion of capital, because the trustor has determined it is in the long range best interests of the beneficiaries that the business be allowed to grow and prosper and that it will eventually repay those beneficiaries. Similarly, certain kinds of investments in land may be "loss leaders" and the trustee may be directed to retain those investments during the loss period for the ultimate benefit of the beneficiaries later. We would hesitate to state that the exculpation language in the document (which is often a necessary precedent before the trustee will agree to act as trustee of such a trust) should be disregarded. Sometimes beneficiaries do have to suffer in the short term to get long term results. We should be cautious about letting a beneficiary who has "suffered" freely sue a trustee for an "excused breach," when the breach of the usual trust duties was performed at the express direction of the trustor in good faith when the trustor had a legitimate long term goal justifying the exculpation and the "breach."

While it may not be codified anywhere in our laws, I believe that California case law condones exculpation of the trustee by the beneficiaries. If nothing else, if all of the beneficiaries knowingly consent to and condone an act, they don't have standing to sue to question that act at a later date. This is also tied to the issue of waivers of accounting to some degree. If consent is knowing, it ought to be binding. In this regard, we agree that the Indiana Trust Code language is a reasonable statement of what the law ought to be, and probably is in practice.

We see no reason to legislate on the issue of laches.

Liability of Trust and Trustee and Non-Beneficiaries - Memorandum 84-24, Study L640

We are concerned with the words "personally at fault" in both proposed Sections 4521 and 4522. We believe that the essence of both of these sections is better stated in the Restatement Second of Trusts. We prefer the language of Restatement Section 265 to proposed Section 4521 and of Restatement Section 264 to proposed Section 4522. We believe that proposed Sections 4530, 4531 and 4540 are an improvement of existing law.

Once again we suggest that the appropriate treatment of creditors' rights to reach the assets of inter vivos trusts created as estate planning vehicles (will substitutes) be addressed. While we believe that the arguments are strong that a power to revoke is essentially equivalent to a general power of appointment and creditors may reach such a trust under Civil Code Sections 1390.3 through 1390.5, we believe that a statutory change which eliminates distinctions and which clarifies the law would be desirable. We believe that a power to revoke should be treated the same as a general power of appointment. While a power to revoke passes with the decedent, so does the power to presently exercise a general power of appointment. We believe that language essentially similar to Civil Code Section 1390.3(b) or 1390.4 should be adequate to allow creditors of the donor-trustor of a revocable inter vivos trust to reach the deceased trustor's assets in that trust. If such a statute is enacted, and we believe it should be, then we believe there should be an optional procedure for publishing a notice of death in order to give the trustee the option of shortening the statute of limitations for creditors' claims. An advantage to allowing such an option is that it does permit the trustee to promptly distribute trust assets to a beneficiary without fear of later problems in dealing with creditors.

We do not agree with the suggestion of Robert A. Schlesinger that formalities for revocable trusts be the same as those for wills.

Office of Trustee - Memorandum 84-26, Study L-640

We are concerned about the provision for a certificate of trustee under § 4550 as it applies to trusts not subject to court supervision. If there is a court file and if that court file shows the incumbency of the trustee, in situations where it is not necessary to go to the court in order to change trustees, the ability of a clerk to issue a certificate based upon the court file may be an invitation to fraud or, at the very least, inaccuracy. The Certificate procedure seems only to be appropriate in situations where there is continuing court supervision of the trust and so it is likely that the court file will be accurate. If the certificate is limited to situations where it may not be abused, it will be limited to an increasingly small minority of supervised testamentary trusts. Under those circumstances, we should consider removing the section altogether.

We approve the codification of a rule that where three or more co-trustees are acting, then the majority may act to bind them.

We believe that the liability of a resigning trustee not only continues, as stated in § 4571, but the term of continuation should be more explicit. We believe that § 4571 should be altered, so that the liability of the resigning trustee is not released or affected in any manner by the trustee's resignation and continues until the trustee is discharged. At the very least, it should continue until the delivery of all assets to a successor trustee or to beneficiaries of the trust upon distribution and a final accounting has been made or waived by all affected beneficiaries.

Section 4574 does not go for enough. A trustee who resigns or is removed from the office not only has the duty to deliver trust property to the successor trustee, but also continues to be responsible for properly administering the trust property prior to its delivery. This ties in with the deficiencies of Section 4571, where it should be clarified that the trustee continues to have the duty to act as trustee until the trust estate has been delivered to the successor trustee or person appointed by the court to receive the property. The resigning trustee's duties continue until a successor is in a position to assume his, her or its duties.

As discussed at the April meeting, subsection 2(b) of Section 4580 should be amended, so that the second sentence reads, "If the trust provides for more than one trustee, unless otherwise provided by the trust instrument, the court may, in its discretion, increase, reduce or maintain the original number of trustees."

The comments contain references to sections regarding discharge of trustee from liability without giving the appropriate section numbers. These sections are not contained in this memorandum, and we did not find where they were contained. We believe some clear definition of when a trustee is discharged from liability to be desirable.

While we understand the necessity of approaching some of these subjects piecemeal in initial stages of analysis, we have noted that it is often difficult to make the necessary cross-references needed to fully understand the new comprehensive article on trust law that will be found in the Probate Code. As the language of the individual studies is refined, we believe it would be quite helpful to consolidate it into one study which would be comprehensive and would allow greater utilization of cross references in a meaningful way.

Judicial Administration, Memorandum 84-29, Study L 640

We believe there continues to be a gap of the jurisdiction of the Superior Court over trust proceedings where a testamentary trust was established under the will of a California decedent, where judicial supervision of trust administration is not necessary, and where the only trustees are individuals who are not residents of California. Since such trusts do not have a principal place of administration in this state under the terms of proposed section 4600, then there appears not to be jurisdiction over the trustee under section 4603, and the availability of venue under 4602(b) appears to be irrelevant. We believe that when a California decedent establishes a trust under his or her will, the California courts continue to have an interest in the proper administration of that trust. If a trustee or successor trustee removes himself or herself from the State of California, the court should not automatically lose jurisdiction over that trust. Currently, there appears to be a loss of jurisdiction, but we believe that gap ought to be filled. If the trustee wants to remove the California testamentary trust to another jurisdiction, the trustee should be required to avail himself of the proceedings to transfer to another jurisdiction.

We believe that subdivision (a) of Section 4618 is sufficient if the material in brackets is removed.

In general, we commend you for attempting to eliminate, to the extent possible, the distinctions between testamentary trusts not subject to court supervision and inter vivos trusts not subject to court supervision.

Transfer of Trust to and from California - Memorandum 84-30, Study L640.

Please refer to our letter dated April 16, 1984 for comments.

Revised Uniform Principal and Income Act - Memorandum 84-32, Study L640

Once again, we refer you to our letter dated April 16, 1984. Since then, we have reviewed the letter of the State Bar Section dated April 25, 1984 and we would like to join in some of their comments. Specifically, we agree that it would be a good idea to renumber and place at the beginning of the Act Section 4816. On the other hand, we question why there needs to be another definition of "Trustee" in the Principal and Income Act when it is already defined in Section 84 of the Probate Code.

We agree that it may be desirable to reverse the "no carry over" rule for income losses of businesses and farming operations in Section 4809. The reasons given in the letter from the State Bar Section are persuasive. Furthermore, that reversal will accord with most trustors' intent and understanding.

Finally, we would like to change the position taken in our April 16, 1984, letter with regard to Section 4801. While we believed it was clear at this point in time that principal and income as defined for probate and trust accounting purposes does not relate to the calculation of income for tax purposes, apparently some attorneys have reported difficulty in convincing agents of the Internal Revenue Service that such is the case. If problems will be encountered with the I.R.S. by omitting this Section from the law, then we should retain Section 4801.

Community Property in Joint Tenancy Form - Study F-521

Although this particular study is not on the agenda for the June 21-23 meeting, we thought we would make some further comments on the study based upon the report to us of the April meeting.

If any such legislation is enacted, and we believe that serious consideration should be given as to whether any of this legislation should be enacted, it should be expressly limited to joint tenancies between husband and wife with no other parties. While joint tenancies between husband and wife and third persons may be the minority, those particular types of joint tenancies create the most difficulties under the proposed legislation. We believe that any attempt to create a conclusive presumption of community property should only apply when the husband and wife are the only parties to the joint tenancy.

If there is any chance that this new rule of law will eliminate the availability of a double step-up in basis under Section 1014(b)(6) of the Internal Revenue Code, it should not be enacted. Currently probate practitioners have ways of getting a determination that property held in joint tenancy title form is in fact community property. The new legal form of community property with survivorship appears to more closely correlate with the common law title of tenancy by the entirety than with the traditional concept of community property. Since tenancies by the entirety are treated like joint tenancy with regard to obtaining a step-up in basis for income tax purposes, it is

possible that this new property ownership situation may have similar problems.

Very truly yours,

Valerie J. Merritt
Secretary Treasurer

VJM:rhy/179

cc: Leslie Rasmussen
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June 20, 1984

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

Dear Commissioners:

On behalf of the California Bankers Association we submit our comments on various studies which are scheduled for discussion at your meeting on June 21-23, 1984.

I. Trustees duties, *memorandum* 84-21, study L640

Section 4300 should include a general statement of the duties of the trustees to properly administer the trust. However, it should not contain a specific list of those duties. A general statement would appear sufficient, and reference to the extensive discussion in the restatement can be made if specificity becomes necessary. Similarly, it is advisable that the statute not contain a list of permissive investments. With deregulation and the multitude of new investment vehicles that are being introduced, a codified list of acceptable investments will be unduly restricted.

Section 4302 should be amended as follows:

> "Unless the beneficiary consents with full knowledge of the facts and without any undue influence on the part of the trustee, a trustee may not use or deal with trust properties for the trustee's own profit or for any other purpose unconnected with the trust, or take any part in any transaction with which the trustee has an interest adverse to the beneficiary, except as provided by law or under the trust instrument".

Section 4303, Duty to Obey Trust should include the provisions of Civil Code §2258(a). Suggested revision is as follows:

> (a) Except as provided in §4401, a trustee shall fulfill the purpose of the trust and follow the directions in the trust except as modified with the consent of all beneficiaries.

California Bankers Association proposes that:

> §4305 be added, entitled "Loans to Third Parties."

> 4305. "A loan by a bank (as defined in §102 of the Financial Code) in the ordinary course of its commercial banking business to a third-party for the purpose of purchasing property which such bank holds in a court or private trust (as defined in §1581 of the Financial Code) shall not constitute an impermissible act of self dealing or conflict of interest in the absence of sufficient evidence thereof."

It should be noted that this provision substantially follows the provision of present Financial Code §3377.1, which allows a bank to make a loan to a trust of which it acts as trustee. Since the legislature has seen fit to allow this type of transaction without a conflict of interest arising, loans to independent third-parties for purposes of purchasing trust real property should similarly not constitute a breach of fiduciary duty.

Section 4320 should be amended in order to add all of the language of present Assembly Bill 630. The provisions of AB 630 should be incorporated in order to provide guidance and protection to all trustees.

Section 4321, Expert Trustees Standard of Care, should be deleted. The proposal would establish different standards for different fiduciaries. The degree of differences is not defined, and no guidances is given to the courts in determining which trustees will be held to the higher standards and which need merely meet a lower standard. Do all attorneys and accountants possess "special skills?" What about an attorney who is not a trust specialist? Is there a higher standard for a businessman than a housewife? What problems of proof will be encountered in trying to prove that the trustor was aware that the fiduciary had "special skills" or that the trustor relied upon those skills in selecting the fiduciary? The general effect of this statute is felt to be very disadvantageous for the beneficiaries of a trust who should be able to expect the highest degree of fiduciary responsibility from any trustee. An individual fiduciary should not be held to a low standard.

Section 4340, Trustees General Duty to Inform and Account to Beneficiaries: This is much too vague.

The confidentiality requirements of the Financial Code §1582(e) should be considered. Revocable trusts should be excluded from the provisions, as a beneficiary of such a trust does not have a right

to information until the trust becomes irrevocable. The accounting language of §4341 appears sufficient. It appears appropriate to combine the provision of 4340 into §4341, which more specifically describes the trustee's duty to account to the beneficiaries. The uncertainties created by §4340 would then be eliminated.

Section 4341, Duty to Account Annually to Income Beneficiary. This provision should be applied to all trusts, thus eliminating the dichotomy between pre 1977- Testamentary Trusts and all other trust. The requirement that annual accountings be forwarded to the beneficiaries of a trust is appropriate. However, §4341(b)(2) requires an inventory of trust property as of the end of the last complete fiscal year of the trust. The accounting period of the trust may very well not coincide with the tax fiscal year end of the trust, as in most situations the statements which are prepared by a corporate fiduciary will be on a calendar year and disseminated on a quarterly basis. Typically, a fiscal year end will occur at some other period during the year. The provision in this section should be amended to require that the inventory of trust property as of the end of the last accounting period be included in the accounting.

Section 4341(b)(3) should require the trustee's compensation for the complete accounting period to be included, instead of the last fiscal period.

§4341(b)(4),(5):

CBA sees no reason for the requirement that beneficiaries must continue to be given the information regarding petitions to the court pursuant to §4620 to obtain a court review of the accounting. Other trust beneficiaries do not receive this information, and yet is well aware of his or her right to obtain judicial review. For this reason, the provisions of proposed §4341(b)(4),(5) should be deleted.

§4341 (c):

The alternative of allowing the trustee to satisfy the requirement of an annual accounting under §4341 by furnishing a copy of the income tax returns pertaining to the trust does not satisfy any actual information requirements which a trustee will have. The tax returns probably will not contain the same information as would be included in the accounting. Further, this subsection seems to permit the trustee to delegate to the accountant the duty to keep the beneficiaries informed. Therefore, it appears that §4341(c) is not an appropriate alternative to a formal annual accounting.

Proposed §4341(f):

The California Bankers Association would like to propose that §4341 be amended to include a subdivision (f) providing a one year statute of limitations for objections to be filed to an accounting, or a four year statute of limitations if no accounting is filed. This provision would be consistent with the statute of limitations provisions under ERISA and should be included in order to give a reasonable period of time within which a beneficiary may complain of a trustee's actions absent fraud.

Section 4350, Discretionary Powers to be Exercised Reasonably

Section 4350 should be amended to include the following:

> 4350. Except as provided in §4531, a discretionary power conferred upon a trustee is presumed not to be left to the trustee's arbitrary discretion but shall not be exercised arbitrarily or capriciously.

Section 4351, Standard for Exercise of Absolute, Sole or Uncontrolled Powers

Section 4351(a) continues discussion of discretionary powers by requiring that the trustee not act in bad faith or disregard the trust purposes. However, the provision appears to conflict with proposed §4478(a), which appears to authorize delegation of some discretion to agents. This conflict should be resolved since the exercise of discretion and potential delegation of discretion under the proposed section is an area that is likely to result in litigation.

Section 4352, Exercise of Power to Discharge Obligtions of Holder

The provisions of §4352 should be amended to clarify that the person who holds a power to appoint or distribute income or principal may not use the power to discharge the person's "own" legal obligations. The insertion of the word "own" would clarify this provision.

II. Powers of Trustees Memorandum 84-22, study L-640

Section 4402, Conflict of Interest in Exercise of Power

The California Bankers Association feels that the consent of benificiaries should allow the exercise of a trust power if there is

a conflict of interest, in addition to the courts determination. Additionally, the specific permission in the trust instrument to exercise such a power should allow the trustee to exercise such a power despite the conflict. §4402(b) should be amended adding §4472 as a section to which the provisions of subdivision (a) do not apply.

Section 4426, Participation in Business; Change in Former Business

The California Bankers Association is concerned with the ownership of general partnerships in a trust. The general concensus is that such general partnerships may not be owned by banks due to the unlimited liability of the trustee. It appears appropriate to add language limiting the liability of the trustee in a general partnership to trust assets of the trust engaged in such partnership. The inclusion of this language in §4426 appears appropriate.

Section 4428, Acquisition of Undivided Interest

Section 4428 should be amended to allow the beneficiary to acquire an undivided interest in trust property, as well as the trustee.

Section 4432, Deposits in Insured Accounts

4432.(a)(1) should be amended to read as follows:

> "An account in any bank to the extent that the deposit is insured or collateralized under any present or future law of the United States or any state where the deposit is located."

§4432(b) should be amended as follows:

> A trustee may deposit trust funds pursuant to subdivision (a) in a financial institution which may be the trustee or an affiliate.

Section 4434, Acquisition and Disposition of Property

Section 4434 should be amended to state:

> "The trustee may acquire or dispose of property for cash or on credit or in an exchange at public or private sale."

Section 4446, Mineral Leases

Section 4446 should be amended to allow the trustee to enter into a lease for a term "beyond the term of the trust." The addition of those words at the end of the section would accomplish this result.

Section 4472, Loans to Beneficiary

This section enhances Financial Code §3377.1 which allows the trustee to make a loan to the trust. The ability of the trustee to make a loan to the beneficiary on adequate security and at a fair rate of interest is appropriate, however, the section should be clarified to indicate whether the trustee personally may make this loan or whether the trust may make the loan. The provision should allow both the trustee personally and the trust to make such a loan.

Section 4478, Hiring Persons

The ability to hire persons should include the ability to hire an accountant.

Section 4478(b) should be amended so that the fiduciary must personally investigate and have responsibility for hiring the second tier of a trustee's responsibility should be carefully considered by the Commission: i.e., Does the trustee have a responsibility to personally investigate the adequacy of an attorney's opinion? If the hiring process was done correctly, the answer is arguably "NO."

III. Memorandum 84-23, Breach of Trust

The California Bankers Association agrees in concept with the recommendations of the Law Revision Commission staff contained in this memorandum. Attached for consideration of the commission are memoranda from Mr. Melvin H. Wilson dated June 11 and June 13, respectively. Please review these memoranda for purposes of further revisions to these provisions. Upon receipt of specific section proposals, the California Bankers Association will comment specifically.

IV. Memorandum 84-24, Liability of Trust and Trustees to Third Persons

Section 4521, Personal Liability of Trustee Arising from Ownership or Control of Trust Estate

This section should be clarified to include specific language indicating for what act the trustee has liability. California Bankers Association suggests that the language be revised as follows; to clarify what "is personally at fault means." Additionally, the section should be amended as follows:

> 4521. A trustee is personally liable for allegations arising from ownership or control of trust property only if the trustee has committed willful misconduct causing loss to the trust.

Section 4522, Personal Liability of Trustee for Torts

Similarly, §4522 should be clarified to indicate for what the trustee is actually liable. The addition of the words "for willful misconduct causing loss to the trust" would clarify the purposes of the Commission in establishing this code section.

Section 4524, Liability as Between Trustee and Trust Estate

The California Bankers Association hopes that the Commission will clarify this provision to indicate that the internal affairs of the trust estate are within the exclusive jurisdiction of the Probate Court. The external affairs of the trust may or may not be subject to the jurisdiction of the Civil Court, but should also be within the jurisdiction of the Probate Court.

The clarification of this section to indicate the Probate Court's jurisdiction over internal matters of the trust would be most helpful. It is suggested that §4524 be amended to state:

> "4524. The question of liability as between the trust estate and the trustee individually, may be determined in a proceeding for accounting, surcharge, or indemnification, under Probate Code § ____."

This provision would clarify to persons seeking redress of trustee's wrongs that the proper arena is within the Probate Court.

It is strongly suggested that an additional section be added regarding a trustee's duty to a beneficiary. The following is proposed:

> "§4525. Trustee's duty to beneficiary is not a duty to a third person."

4525. A duty owed by a trustee to a beneficiary by reason of a trustee acting in such capacity shall not be imputed as a duty owed to a person who is not a beneficiary."

This proposed provision would clarify the position of the trustee vis-a-vis a creditor of the beneficiary. Except under the conditions of a garnishment, which is appropriate, a creditor should not be able to attack a trust for the beneficiary's debts, and should not have the ability to interfere in the trust's internal affairs. This provision would alleviate the trust's expensive involvement in litigation in which it is not an appropriate party.

Section 4531, Trustee's Lien

Section 4531 should be amended to state:

4531. The trustee has a lien on the trust property as against the beneficiary in the amount of advances, with any interest, made for the protection of the trust or for trustee's compensation, expenses, losses, etc.

Section 4544, Effect on Real Property Transactions Where Beneficiary Undisclosed

Section 4544(a) perpetuates a problem of former Civil Code §869a.

One problem banks have encountered with Civil Code §869a is the requirement that a beneficiary be "indicated in the instrument." This seems to require that a beneficiary be identified in the conveyance. It is fairly common practice for conveyances to trustees to use the following terminology: "Zuma Beach Bank as trustee for trust #12345" or "John Q. Jones, trustee of the Smith family trust dated June 11, 1984." Both forms indicate that there is a specific, identifiable trust agreement under which the trustee acts, but the identity of the beneficiary can only be determined by inspection of the governing instrument.

In view of the desirability of confidentiality in intervivos trust arrangements, the statute should clearly indicate that an indication of the instrument establishing the fiduciary relationship should suffice. Suggested wording would be:

§4544. "If an interest in or lien or encumbrance on real property is affected by an instrument in favor of a person in trust and neither the identity of the instrument establishing such trust nor beneficiary is indicated in the

instrument, it is presumed that the person holds the interest, lien or encumbrance absolutely and free of the trust."

V. Memorandum 84-26, Office of Trustee

Attached is a letter dated June 14, 1984 from Mr. Bruce Steele, Office of Trust Counsel at First Interstate Bank, regarding memorandum 84-26. These comments are incorporated herein by reference. Of specific concern is the need for an exemption of a corporate trustee from the bonding requirements. The state's Corporate Ttrustee reserve requirements adequately protect trusts, and no additional Bond is necessary.

Section 4560, Actions by Co-Trustees

Section 4560 should be amended to require the unanimous decision of the trustees for a power to be exercised. The tax consequences of non-adverse parties making decisions binding the adverse party are serious. The corporate trustee could be bound by an act which is contrary to the trust instrument. A careful study is recommended of this area, due to the difficult problems in the investment area as well as the liability of the dissenting trustee if a majority may rule. At the very minimum, the dissenting trustee should be exculpated of liability. The duty to stop an act which is contrary to the provisions of the trust or which is a breach of fiduciary duty in the opinion of the dissenting trustee, should also be carefully reviewed.

Section 4561, Inability of Co-Trustee to Act

This section should be amended in order to clarify the co-trustee's ability to act during situations when the incapacitated co-trustee is unable to act. Suggested revised language follows:

> 4561. Except as otherwise provided in the trust, if a co-trustee dies, is incapable of acting for any reason, resigns, disclaims or is discharged, the remaining co-trustees may act.

This revision would facilitate the on-going administration of a trust even during the temporary absence of a co-trustee.

Section 4570, Resignation of Trustee

Present §1138.8 is the preferred statutory provision regulating the resignation of a trustee. If a trustee wishes to resign, the trustee should have the ability to do so. The court should not have

the ability to force a trustee to do something it does not wish to do. The study within 4570 does not appear to speak to the liability of a trustee for appointment of a successor trustee who may not be competent.

4570(a)(2) should be amended to allow the consent of a majority of the beneficiaries, if they have capacity to give consent, to change trustees.

Section 4572, Removal of Trustee

Section 4572(a) should be amended so that only a trustee, a beneficiary or a remainderman may petition the court for removal of the trustee. The draft presently proposed by the Commission would allow a creditor of the beneficiary or a creditor of the trust to petition the court for removal. It does not appear that this is the intent of the Commission, and specifying the persons who may petition the court appears to be the appropriate cure.

Section 4572(c) should also be amended so that a beneficiary, a co-trustee or a remainderman may petition the court for removal of trustee.

Again, these appear to be internal matters of the trust, and a creditor of the beneficiary should not be allowed to intervene.

Section 4573, Occurrance of Vacancy in Office of Trustee

It is suggested that a subdivision be added to §4573 creating the express authority for the trustee who has resigned to continue to exercise its trust powers during the interim between resignation and appointment of a new trustee and transfer of trust assets and to continue to receive compensation during such period. Otherwise there is a time interim in which the trust assets may not be appropriately subject to trustee control, and harm may occur to the trust assets in such interim.

Section 4580, Appointment of new Trustee

Subdivision (a)(1) should be amended to read:

> "In accordance with the terms of the trust, if the trust provides for the appointment of, or a practical method of appointing a trustee."

This technical change is designed to reflect the fact that when a trust instrument names a person or corporation as successor trustee, this does not create a "practical method" of appointing a trustee, but is an actual "appointment of a trustee."

Subdivision (b) should be changed to read substantially as follows:

> "The court may, in its discretion and on petition of a co-trustee, beneficiary or remainderman appoint one or more trustees to fill the vacancy. In selecting a trustee, the court shall give consideration to any expressed wishes of the beneficiaries."

There does not appear to be any good reason to limit the court's ability to appoint the number of trustees that the court determines to be appropriate under the circumstances.

VI. Memorandum 84-29, Judicial Administration of Trust

Please review the enclosed comments drafted by Melvin H. Wilson with respect to the Judicial Administration of Trust.

Section 4180 should be amnded to be applicable to all testamentary trusts. The California Bankers Association is of the opinion that the trusts should all be treated in a like manner.

The California Bankers Association strongly recommends a policy statement in Section 4630 indicating that whether a complaint or a petition is filed, if it relates to the internal affairs of a trust, there is exclusive equity jurisdiction, and the equity rules will apply. The Superior Court sitting in Probate has the jurisdiction and expertise to handle equity and civil matters. Therefore, it should be made clear that it does not matter what original forum is chosen, the equity rules will apply.

VII. Memorandum 84-30, Transfer of Trust To or From California

The California Bankers Association is in accord with the general recommndations of the staff with respect to transfers of trusts to or from California.

VIII. Memorandum 84-32, Revised Uniform Principal and Income Act

Attached is a memorandum dated 6-18-84 regarding the staff's proposed revision of the California Uniform Principal and Income Act. The California Bankers Association requests the staff to review this memorandum with proposals for amendments to the draft sections.

Section 4810, Natural Resources

Section 4810(a)(3) should be amended to incorporate a reasonable standard in determining the percent of gross receipts to be added to principal as an allowance for depletion. The California Bankers Association realizes that the 27 1/2 standard which is included in the draft is based upon tax standards, however, these standards may vary in the future, and a reasonable standard should be utilized which would be able to take into account any future tax legislation.

Section 4815, Reserve Or Allowance for Depreciation or Depletion

This section should be clarified to indicate that a reserve which is established for depreciation or depletion does not need to be set aside into a separate account by the trustee. Instead, the reserve amounts should be able to be reapplied to the principal corpus of the trust and invested at any manner. Because the end result of the reserve is to benefit the remaindermen, a commingling of reserve amounts with the corpus of the trust is cost effective and appropriate.

A suggested revision of the draft follows:

> 4815.(a). . . .Nothing in this part prevents a trustee in its absolute discretion from establishing such reserve or allowance, or from continuing any previous practice of maintaining such reserve or allowance. Such reserve or allowance need not be separately invested or accounted for. The provisions of paragraph (2) of subdivision (a) . . ..

The California Bankers Association did not receive memoranda 84-31, 84-34, 84-45, 84-51, and 84-57 in sufficient time to formulate formal comments. Comments will be forwarded to the staff at a later date.

With respect to memorandum 84-51, the California Banking Association strongly urges the Law Revision Commission to defer the effective date of the amendments to the Probate Code until such time as all amendments have been enacted. In this regard, The California Bankers Association is in complete accord with the State Bar Association.

Thank you for the opportunity to comment with respect to the memoranda and staff drafts. The California Law Revision Commission staff has done a remarkable job in the work completed to date.

Respectfully submitted,

Paulette E. Leahy
Chair, Trust State Governmental Affairs Committee
California Bankers Association

cc: Committee Members
Blair Reynolds

EXHIBIT 5

MEMORANDUM NO. 7

CLRC Study L-640

To: Paulette Leahy

From: Melvin H. Wilson

Date: June 14, 1984

Subj: Summary of My Memoranda and Modifications to Proposed Statutes

A. Part 4, Judicial Administration Of Trusts, §§4600-4636

1. §4630 See my Memorandum No. 1. The changes in the proposed statutory language that I propose here is slightly different from that proposed in that memo.

a. Subsection (a) should be amended to read as follows: "A trustee, beneficiary, or other interested person may commence a proceeding under this article concerning the internal affairs of a trust or to determine the existence of a trust.

b. A new §(b)(6) should be inserted to read: "(6) Compelling a trustee to redress a breach of trust." The remaining ¶¶ should be correspondingly renumbered.

2. §4631 See my Memorandum No. 1. The changes in the proposed statutory language that I propose here is slightly different from that proposed in that memo.

a. §4631 should be amended to read as follows: "A proceeding under this article is commenced either by filing a verified petition stating facts showing that the petition is authorized under this article or by a complaint which alleges facts which indicate that at least part of the relief sought concerns the

internal affairs of a trust or to determine the existence of a trust."

3. §4635 See my Memorandum No. 1.

a. Insert after (f) a new (g) to read as follows: "(g) Compelling a trustee to redress a breach of trust." The remaining ¶¶ should be correspondingly relettered.

b. Insert after the word "petition" in ¶(1) the words "or complaint."

B. Part 4, Judicial Administration of Trusts - Procedure. See my Memorandum No. 3. Since no proposed statutes are included in the material I have reviewed, my suggestions are only conceptual. The suggestions relate to the need to perpetuate present §§1230-33 (suitably modified) to insure understanding of which rules of procedure are applicable to trust proceedings. In addition, and a point I believe is most significant, is the need to include in the new law a clear statement that the remedies which a beneficiary has against a trustee arising out of a proceeding pertaining to the internal affairs of a trust shall be governed by the principles of the common law applicable in equity proceedings.

C. Chapter 4, Transitional Provisions, §§4180-4186. See my Memorandum No. 2.

1. §4180 should be amended to read: "This article applies to testamentary trusts created by a will executed or republished at any time prior to or after the effective date of this article."

2. §4181(a) should be amended to read as follows:

(a) Except as provided in Section 4182, the trustee of a trust described in Section 4180 shall give a notice on or before [a date which is six months after the effective date of enactment], or within six months after the initial funding of the trust, whichever

occurs later, to each beneficiary, including all persons in being who shall or may participate in the principal or income of the trust. Notice shall be sent by registered or certified mail or by first class mail to the persons to be notified at their last known address. Notice may be sent by first class mail only if an acknowledgment of receipt is signed by the beneficiary and returned to the trustee.

3. §4181(b) should be amended to read as follows:

(b) The notice shall contain the following:

(1) A statement that as of [the effective date of enactment], the Probate Code was amended to terminate mandatory court supervision of the trust.

(2) A statement that Section 4630 of the Probate Code gives any beneficiary the right to petition a court to determine important matters relating to the internal affairs of the trust.

[¶¶(3) through (6), inclusive to remain unchanged]

4. §4181(c) to remain unchanged.

5. §4182 should be amended to read as follows: "The trustee of a trust which was not subject to continuing jurisdiction of the superior court on [the effective date of enactment] shall not be required to give the notice specified in Section 4181."

6. §4183 and 4184 to remain unchanged.

7. §4185 should be amended to read as follows: "It is the intent of the Legislature in enacting this article that the administration of trusts subject to this article shall proceed expeditiously and free of judicial intervention but shall be subject to the jurisdiction of the courts of this state when such is invoked pursuant to this article or

otherwise invoked pursuant to law. If the instrument establishing the trust manifests an intention of the testator that specified internal affairs of the trust, including by way of example, approval of trustee's compensation, shall be subject to judicial review and approval, this section shall not be construed to preclude an interested person from invoking the jurisdiction of the court to comply with such intent."

8. §4186 could be amended to incorporate the second sentence of §1138.4 which exempts pre-July 1, 1977 trusts which were formerly subject to continuing jurisdiction under §1120 from filing fees for petitions filed under §1138.

D. Chapter 4, Relations With Third Persons, §§4520-4544.

1. §4525. See my Memorandum No. 1, page 2. §4525 should be added to read as follows:

"§4525. Trustee's duty to beneficiary is not a duty to a third person

4525. A duty owed by a trustee to a beneficiary by reason of the trustee acting in such capacity shall not be imputed as a duty owed to a person who is not a beneficiary."

2. §4531. See my Memorandum No. 5. Insert after the words "in the amount of": "the trustee's compensation and of"

3. §4544. See my Memorandum No. 5. The first sentence of §4544(a) should be amended to read as follows: "(a) If an interest in or lien or encumbrance on real property is affected by an instrument in favor of a person in trust and neither the identity of the instrument establishing such trust nor beneficiary is indicated in the instrument, it is presumed that the person holds the interest, lien or encumbrance absolutely and free of the trust."

E. Chapter 1, Duties of Trustees, §§4300-4396. See my Memorandum No. 4.

1. A new §4305 should be added to read as follows:

"§4305. Loans to third parties

4305. A loan by a bank (as defined in Section 102 of the Financial Code) in the ordinary course of its commercial banking business to a third party for the purpose of purchasing property which such bank holds in a court or private trust (as defined in Section 1581 of the Financial Code) shall not constitute an impermissible act of self-dealing or conflict of interest in the absence of sufficient evidence thereof."

F. Breach of Trust, no specific statutes proposed. See my Memorandum No. 6, which provides some comments on the consequential compensatory and punitive damage issues.

3816t

ESTATE PLANNING, TRUST AND PROBATE LAW SECTION
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June 20, 1984

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
4000 Middlefield Road, Suite D-2
Palo Alto, California 94306

Re: L-640 - Trusts

Dear Mr. DeMoully:

This letter is a supplement to my letter of April 25, 1984. That letter discussed some of the memoranda being considered at the April meeting of the Law Revision Commission. Since that time, members of our section have studied additional memoranda and have submitted reports on them. The Executive Committee of the Estate Planning, Trust and Probate Law Section has adopted in whole or in part many of those reports as representing the position of this Section. For your convenience, those reports have been synthesized in this letter, and edited to highlight comments which are especially important. Accordingly, this letter represents not only the views of our Executive Committee, but also the views of a number of attorneys throughout California.

Trustee's Duties - Memorandum 84-21

Our comments are detailed in my letter to you of April 25, 1984. We have not seen any supplemental memoranda which would cause our comments to be altered.

Trustee's Powers - Memorandum 84-22

Our comments are detailed in my letter to you of April 25, 1984. We have not seen any supplemental memoranda which would cause our comments to be altered.

One of our members has raised the question of whether or not the trust recommendations are intended to be

prospective or retroactive; that is to say, will they apply to existing trusts? Obviously, if the powers are to be applied retroactively, then existing trusts are not likely to limit them. Thus, there may be a constitutional problem. If the powers apply prospectively, practitioners and trustees are then confronted with two sets of laws. After folding these two sets of laws into the dual sets of laws resulting from new rules of construction, inheritance rights, etc. enacted by AB 25, the number of possible permutations for the application of any law to trusts becomes mindboggling. We submit that this may be one of the more compelling reasons to defer the effective date of AB 25 until all of the Probate Code changes are enacted. We urge the Law Revision Commission to give serious consideration to recommending deferral until the entire package is complete.

Breach of Trust - Memorandum 84-23

It makes sense to consolidate all rules concerning breaches of trust, and to bring more order to the rules. Nonetheless, trust beneficiaries are not as powerless as the Memorandum may suggest and it should be realized that there are avenues already available to beneficiaries. For example, the Memorandum seems to ignore the process available through current Probate Code, Sections 1138 et seq.

As to the proposed statutory list of remedies (contained on page 10), we have several comments. First, we are concerned about the references to the "common law." Is the staff satisfied that common law rules do not conflict with rules of California law or does the staff mean for common law rules to override current California law? At the same time, it is possible that California law may not completely cover some areas of remedies contemplated. Second, an explanation should be added to subsection (b)(9) stating what rights there are in trust property that has been traced. Third, if the proposed statutory language is meant to encompass the exclusive procedures to be used, then the statute needs to go much farther than it does; it would be difficult to elaborate a satisfactory all-inclusive group of exclusive procedures.

Specific indications of statutes of limitations rules that would apply should be set forth.

In trust litigation (as with other litigation) there appear to be two conflicting policies of whether or not attorneys' fees should be allowed. This is especially true in breach of trust cases. Allowing attorneys' fees may encourage

litigation in a field in which litigation is already burgeoning. On the other hand, without some provision for allowance of attorneys' fees, the access of a beneficiary to the Court process may be too restricted. If the trustee is allowed fees from the trust, the beneficiary pays all fees. Perhaps allowing the Court to order the trustee to pay the beneficiary's attorneys' fees would provide reciprocity. Punitive damages do not appear to be a reasonable solution to the attorneys' fee problem if the trustee acts in "good faith" but is found guilty of a breach. Perhaps the Court, in its discretion, should have authority to award or deny attorneys' fees.

The punitive damages question should also be studied. The rules for punitive damages should be more specifically set forth than at present, and fraud which would justify an award of punitive damages should be fraud as generally understood, and not fraud as defined in Civil Code §2234.

Judicial Administration - Memorandum 84-29

The two major questions involved are jurisdiction and venue. With respect to jurisdiction, the basic issue is: to what department of the superior court (probate or non-probate) must a beneficiary bring claims of breach of trust? The staff analysis does not focus and makes no recommendation on the jurisdictional issue.

The issue which is posed in Memorandum 84-29 is dealt with by proposed §§4601 and 4630. Section 4601(a) provides that the "superior court" has "exclusive jurisdiction of proceedings concerning the internal affairs of trusts". Section 4630 amplifies this grant of exclusive jurisdiction by providing that a court proceeding may be brought to "pass on the act of the trustee, including the exercise of discretionary powers". But §4601(b) grants the superior court "concurrent jurisdiction" over "other actions and proceedings involving trustees and third parties". If these sections provide that the superior court sitting in probate has exclusive jurisdiction to review the acts of the trustee and award damages to the trust and to the beneficiaries if they are personally injured by the trustee's action, our concern is unfounded. However, the proposed statute is not clear on this point.

The problem is illustrated by the recent appellate decision in Pitzer v. Security Pacific National Bank, 2d Civ. No. 67448 (2nd Div., May 16, 1984) (certified for publication). In Pitzer, the trial court consolidated a civil action brought by the testamentary trust's beneficiaries against the trustee,

individually, for breach of trust, seeking monetary damages for emotional distress and punitive damages for oppressive, fraudulent or malicious management of the trust, with a probate proceeding rising out of objections filed under Probate Code §1120 by the same beneficiaries to the trustee's accounting. The two matters were heard concurrently before the jury. The trial court found that certain, but not all, of the trustee's conduct constituted a breach of trust and awarded a $25,000 surcharge for damages to the trust. In the civil action, however, the jury found the trustee had breached its trust and assessed compensatory damages for emotional distress to the beneficiaries, individually, consequential damages to certain of one of the beneficiary's properties and punitive damages.

On appeal, the court held that superior court sitting in probate has exclusive jurisdiction over a beneficiary's complaint for breach of trust. It held that under §1120, a separate and distinct legal (as opposed to equitable) cause of action does not arise or exist as a result of an alleged breach of trust of a testamentary trust. The court seems to hold that any award of punitive or compensatory damages based upon some breach of duty to the beneficiaries, individually, was improperly granted by the probate court as beyond its jurisdiction. But, what court has that jurisdiction?

While the Pitzer decision deals with the fundamental issue of the scope of the probate court's jurisdiction to adjudicate civil cause of action, the opinion has complicated the unresolved issue of whether the probate court that has exclusive jurisdiction in a surcharge action also has exclusive jurisdiction to adjudicate the claims of beneficiaries for consequential personal damages which may result from a trustee's conduct which is also the basis for the surcharge.

Both trustees and beneficiaries require guidance on which court has jurisdiction to determine this second issue. The Probate Code should clearly provide that the remedies of the beneficiary against the trustee are to be exclusively adjudicated by the probate court, which would have the authority to grant not only surcharge damages for injury to the trust, but also compensatory and punitive damages to the beneficiaries.

With respect to venue, the staff suggests that the dual venue provisions of present law should be eliminated in favor of "a rule pointing to one court at a given time." The

dual venue rule was enacted to prevent forum shopping by corporate trustees, whose practice has been to transfer trust administration responsibilities from county to county. Typically, corporate trustees have consolidated trust administrative responsibilities to reduce operating expenses and keep trustee's fees competitive. There are few objections to such a procedure, so long as the rights of trust beneficiaries are not adversely affected. Preserving venue in the county in which the probate estate was administered allows the trust beneficiary access to the local court. Thus, the trust beneficiary can avoid the costly alternative of either hiring a new attorney who is unfamiliar with the trust or of paying his present attorney to travel to a distant court. If the staff believes that a one-court venue is appropriate, then it should be the court in which the estate was administered.

Conduct of Trust Business and Qualification by Foreign Trustee - Memorandum 84-27

Foreign Trustees - Memorandum 84-28

These two memoranda inter-relate, and are therefore considered together.

We have serious concerns about permitting foreign trustees to handle trust business in California. It should be clearly understood that our concerns do not stem from any particular desire to protect our local banks, but rather to protect our clients. First, many attorneys now experience a problem with trusts where the corporate trustee states that it cannot give answers to a beneficiary's inquiries since all the records are kept elsewhere. We envision the same problem being exacerbated when a foreign bank announces that it cannot answer the questions of a California beneficiary because all the records are kept in New York. We also envision that there will be removal of trust litigation to the head office of the corporate trustee, which will inconvenience California Trustors and beneficiaries. This concern can be solved by enacting coordinating Civil Procedure Code sections to require that the foreign trustee be subject to California jurisdiction and that jurisdiction cannot be removed to another state for the convenience of the trustee, unless all beneficiaries consent.

The memoranda seem to imply that California testators cannot name foreign banks as trustees. Indeed, many of our clients name banks in other states and provide that the trust will be governed by the law of that particular state. We have had no problem with such arrangements. If there is

real property in a trust, an additional problem is presented, but can be easily solved by naming an individual trustee who will hold title to foreign real property. This works whether it is a California trust holding foreign real property or an out-of-state trust holding title to California real property.

There is also some concern about jurisdiction of a foreign trust in California where the foreign corporate trustee qualifies for doing business. If a Nevada bank were named as trustee with the testator and the income beneficiaries being California residents, would the trust be subject to Nevada law or California law?

In order for a foreign corporate trustee to do business in California, it should be required at a very minimum to keep all trust records in California. Further, no California jurisdiction should be obtained against a trust which is otherwise located out of California solely because the corporate trustee is allowed to do business in California.

In summary, we are opposed to allowing foreign corporate trustees to act as trustees in California unless there are very tight rules and regulations which require that (1) the trust documents and records be kept in California; (2) California does not acquire jurisdiction over to a foreign trust solely by reason of the foreign trustees doing business in California; and (3) there should be no change of jurisdiction in the event of trust litigation.

Presumption of Revocability of Foreign Trusts - Memorandum 84-34

We approve the general approach suggested by the staff, with the following specific comments.

First, the term "resident" should be defined. For example, a California domiciliary may have a summer "residence" in another state, and enter into a trust agreement in California. Will the question of revocability be determined by the law of California? Would the answer to that question depend upon whether the trust agreement were signed in California or in the other state? Would it depend on whether the trust agreement were signed during the summer (while resident in another state) or during the winter? Those questions can be eliminated by substituting the word "domiciliary" for "resident" in §4201(a).

Section 4201(b) should provide that the law of the other state as to revocability applies if "the intention of the trustor cannot be determined from the provisions of the trust." The obvious question is that, in such circumstances, should not the law of the other state apply to all aspects of the trust (e.g., rules of construction, rights of beneficiaries, etc.) and not be limited to revocation, except where California real property is concerned?

The title of §4201 should not refer to "presumption" but rather be entitled "Revocability of Trusts."

We believe that oral express trusts should never be irrevocable, and that the first clause of §4201(a), "Unless expressly made irrevocable by the instrument creating the trust," should be retained.

Very truly yours,

Kenneth M. Klug