#L-618 12/24/84

Memorandum 85-16

Subject: Study L-618 - Uniform Transfers to Minors Act

Attached is a letter from John W. Schooling (Exhibit 2) suggesting that a provision of former law be restored to the new California Uniform Transfers to Minors Act. Former law permitted a transferor (one who creates a custodianship of property for a minor) to designate one or more successor custodians in the same document that transferred the property into the custodianship. The text of the former provision is set out as Exhibit 3. This provision is not found in the official version of the Uniform Transfers to Minors Act and was not continued in the new California Uniform Transfers to Minors Act.

The staff agrees with Mr. Schooling that the transferor should be able to designate, at the time the custodianship is created, successor custodians in case the original custodian is unable, declines, or is ineligible to serve or resigns, dies, becomes incapacitated, or is removed. It is sound public policy to permit the transferor to determine who is to serve as a successor custodian. The transferor is the one who creates the custodianship. The transfer's preference as to the substitute custodian should have preference over a substitute custodian selected by someone else. Attached as Exhibit 4 is a staff recommended revision of the California Uniform Transfers to Minors Act to restore the substance of the provision of prior law. The staff draft makes one modification of prior law. Prior law permitted a successor custodian to be designated by the transferor only in the document that created the custodianship; the staff recommended revision permits that and also permits use of a separate document executed as a part of the same transaction that created the custodianship and contemporaneously with the execution of the document that created the custodianship.

The staff believes that there should be no delay in making the revision suggested above. Accordingly, the staff suggests that the Commission approve an appropriate provision to accomplish the objective of the staff recommended draft and that the provision be included in a bill introduced at the 1985 legislative session.

Mr. Schooling makes an additional suggestion in his letter and a number of additional suggestions in his excellent article (attached as Exhibit 1). If the Commission desires, the staff can prepare an analysis of these other suggestions. However, since we have decided to prepare a new Probate Code for the 1986 legislative session, the staff recommends that consideration of these other suggestions be deferred until after that project is completed. The staff believes that Mr. Schooling's other suggestions merit careful study. But, if we are to have a new Probate Code for 1986, we cannot now devote staff resources and Commission time to the consideration of these other suggestions.

Respectfully submitted,

John H. DeMoully
Executive Secretary

EXHIBIT 1

Memo 85-16

CALIFORNIA CONTINUING EDUCATION OF THE BAR

ESTATE PLANNING & CALIFORNIA PROBATE REPORTER

Volume VI, Number 2, October 1984 Page 21

HIGHLIGHTS

California's Modified Version of the New Uniform Transfers to Minors Act

by John W. Schooling

Have you found the California Uniform Gifts to Minors Act (CC §§1154-1165) to be of significant use in your practice? Probably not. Have you found the Act's usefulness increased by the repeated legislative attempts to fix it? Probably not. But California's modified version of the new Uniform Transfers to Minors Act (CUTMA) (Stats 1984, ch 243), effective January 1, 1985, completely overhauls and expands the law of custodianships for minors, providing a much more useful estate planning tool. Equally important, the new Act will apply to many estate planning situations even though it is not specifically invoked. Accordingly, practitioners must understand the new law even if they do not wish to use it.

Under CUTMA the classes of transfers which may be made to custodianships include such diverse transfers as trust distributions, payment of insurance proceeds, and payments of debts. It also contains provisions permitting custodianships for some types of transfers to remain in effect to age 21 or 25. Finally, there are situations in which an estate, trust, or life insurance company may make a distribution to a custodian for a minor even though the governing instrument does not authorize such a distribution. This article outlines the provisions of the new law and discusses some of the problems it presents.

Background

California custodianships originated with the 1955 enactment of the California Gifts of Securities to Minors Act. Stats 1955, ch 1958, §1. The law was expanded and renamed the Uniform Gifts to Minors Act (UGMA) in 1959. Stats 1959, ch 709, §2. The UGMA was amended in

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1961, 1963, 1965, 1968, 1969, 1970, 1972, 1979, 1980, and 1982, with each amendment adding some clarification or extension. In 1983, provisions were inserted in Prob C §§6340-6349 to permit devises by will to be made to UGMA custodianships effective January 1, 1985. In making these amendments, California has been a leader in the area. It was one of the first states to remove limits on the types of property custodianships could receive and to allow use of the Act by will. The new law repeals the UGMA and supersedes it with a statute that will be codified as Prob C §§3900-3925.

The CUTMA was influenced by the National Conference of Commissioners on State Laws, which had earlier recognized that the UGMA, one of its most successful products, had become quite nonuniform. Many states like California had undermined uniformity by taking repeated legislative action to correct deficiencies. As a result, the commissioners promulgated the much broader Uniform Transfers to Minors Act in 1983 (the Uniform Act).

This Uniform Act was reviewed and revised by the California Law Revision Commission, and was subjected to many amendments during the legislative process. Of course, this detracts from the goal of uniformity, but the California changes resulted in significant advances, most notably a careful, flexible treatment of the age at which a custodianship may terminate.

Structure of the Act

A. How Transfers Are Made

The CUTMA contains specific language to be used in transferring property to a custodianship. Prob C §3909. If termination beyond age 18 is desired, the forms must contain additional language to that effect. Prob C §3920.5. Thus, for example, a life insurance beneficiary designation intended to impose a custodianship until the beneficiary attains the age of 25 should read: "John Doe as custodian for Mary Doe until age 25 under the California Uniform Transfers to Minors Act." Prob C §§3903, 3920.5.

There are several safety features in the Act to cure drafting errors, including provisions permitting the language of transfer to follow Prob C §§3909 and 3920.5 "in substance," and validating transfers purporting to be made under the former UGMA or made incorrectly under the laws of another state. Prob C §3922. Further, Prob C §3923 makes clear that transfers not expressly authorized under the UGMA are valid if they are valid under the new law.

B. Situations in Which Transfers May Be Made

The former act primarily applied to gifts. The CUTMA creates new circumstances under which a transfer to a custodianship may be made, and there is clarification of some old questions. Most significantly, Prob C §3903(a) provides that "[a] person having the right to designate the recipient of property transferable upon the occurrence of a future events may revocably nominate a custodian to receive the property for a minor beneficiary upon the occurrence of the event."

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This authorization is broad enough to permit naming a custodian in wills, trusts, instruments exercising powers of appointment, insurance policy and employee benefit beneficiary designations, P.O.D. accounts, or any other right to future payment. Even though such a designation is not itself a transfer under the Act and does not immediately create custodial property, if unrevoked at death it becomes operative. This is a major expansion of former Prob C §6340, which only applied to wills. Another significant expansion permits a transfer to be made to a person who is no longer a minor if the custodianship is to continue to an age permissible under the Act and not yet attained by the transferee. Prob C §3901(k).

New Prob C §3906 is particularly important for estate planners. This provision authorizes personal representatives and trustees to transfer property to a custodianship for a minor even though the governing instrument contains no express authorization for such a distribution or a decedent has died intestate. Three requirements must be satisfied: (1) The personal representative or trustee must consider the transfer to be in the best interest of the minor, (2) the transfer must not be prohibited by or inconsistent with the governing instrument, and (3) the court must approve the transfer if the amount transferred exceeds $10,000. Such a custodianship must terminate at age 18.

Probate Code §3904 restates current law by authorizing present transfers to custodianships by gift. The language of the statute includes irrevocable exercises of powers of appointment. Probate Code §3909(a)(4) makes clear that gifts can include the irrevocable transfer of a present right to future payments. This includes royalties, promissory notes, interests under life insurance contracts, and the like.

The CUTMA also provides for use of a custodianship in lieu of a guardianship in some instances. Thus, when a minor has a guardian and the sole asset to the guardianship is money, the court may terminate the guardianship and transfer the funds to a custodian. Prob C §3412(b). Previously, this was only permitted by inference and only for $20,000 or less. Otherwise the only alternative was to use a blocked account. Under Prob C §3413, the same rule applies even if no guardian has been appointed. Furthermore, Prob C §3611(c), concerning minors' compromises, will allow transfer of any kind of property to a custodian.

A particularly novel provision is Prob C §3907, which permits a transfer to a custodian by a person who holds a minor's property or who owes a debt to a minor. The section, however, is limited to transfers not exceeding $10,000 unless there is a valid nomination of a custodian under Prob C §3903 (*e.g.*, a custodian was named in a life insurance beneficiary designation). If no custodian was designated, the custodian must be an adult member of the minor's family (parent, stepparent, spouse, grandparent, sibling, aunt, or uncle).

It is also clear that emancipated minors may make transfers to custodianships by gift or will under CC §63(b)(5), (6), as Prob C §3901(p) does not require the transferor to be an adult. In fact, a minor transferor may be a custodian—an exception to the general rule that custodians must be adults. Prob C §3909(a). Report of Senate Committee on Judiciary on Assembly Bill 2492, Senate Journal, June 14, 1984, p 11795.

C. What Property Can Be Transferred to a Custodian?

It is intended that any type of property may be transferred to a custodian. The fact that some of the old definitions of certain types of property have been omitted is not to be considered a limitation. The comments in the Senate Judiciary Report specifically state the omission is because these definitions are unnecessary (pp 11794-11795). Custodial property is expansively defined in Prob C §3901(f) to include "(1) any interest in property transferred to a custodian under this part and (2) the income from and proceeds of that interest in property." The comments to the proposed Uniform Act are adopted here to indicate that this expanded definition should "encompass every conceivable legal or equitable interest in property of any kind, including real property and tangible or intangible personal property." National Conference of Commissioners on Uniform State Laws, "Uniform Transfers to Minors Act," p 6. This includes interests in joint tenancies, irrevocable beneficiary designations under insurance policies, and land in other states, even if the other state has not adopted the Act. This broad intent is further evidenced by a catchall provision in Prob C §3909(a)(7) providing for transfer of an interest in any property not described in Prob C §3909(a)(1)-(6).

D. Age of Termination

A custodianship terminates at the earlier of age 18 or the death of the minor unless the terms of its creation delay termination under Prob C §3920.5. This new provision, more than any other, makes a custodianship a vehicle clients will be willing to consider. Generally, custodianships created by trust distributions and transfers taking effect at death may remain in effect until a date specified in the creating instrument, but not beyond the date the minor attains the age of 25.

Custodianships created by inter vivos gift cannot remain in effect past age 21. This limitation on gifts is intended to prevent inadvertent loss of the gift tax annual exclusion by conforming the custodianship to the provisions of IRC §2503(c).

Custodianships that are essentially substitutes for guardianships (rather than substitutes for express trusts)

must end at age 18. This includes custodianships created under Prob C §§3412 (money transferred from guardianship), 3413 (court ordered disposition of minor's money when there is no guardianship), 3602 and 3611 (minor's compromise), 3906 (transfer by personal representative or trustee in the absence of an express authorization in a governing instrument), and 3907 (debtor of minor or person holding property of a minor where the minor has no guardian).

If an older age than is permissible is inserted in a document, the transfer is valid, but the custodianship will still terminate at the maximum age permitted by the statute for the particular type of transfer. Prob C §3920.5(g).

E. Who Can Be the Custodian?

Generally, the custodian may be any adult or trust company. This rule is subject to some exceptions. In some cases the transferor cannot be the custodian (*e.g.*, a transfer of untitled tangible personal property). In other cases the transferor can be the custodian only if specific formalities are complied with (*e.g.*, if the transferor is custodian of property titled by a state agency, it is insufficient merely to endorse the title—a new title must be obtained as evidence of the transfer). Such limitations on transferors acting as custodians appear to result from the need for a means of proving a transfer has actually occurred. The requirements for transfering specific types of property are contained in Prob C §3909.

There are other limitations on the identity of the custodian. As noted above, an emancipated minor cannot be a custodian unless he is also the transferor; in the absence of a designation, an adult family member or a trust company must be the custodian of a custodianship established under Prob C §3907 by a person owing a liquidated debt to a minor.

F. Substitute and Successor Custodians

The provisions for alternate custodians are significantly changed under the new Act. The new law distinguishes between "substitute" custodians and "successor" custodians. A substitute custodian becomes the custodian if the originally named custodian never takes office. This is most likely to occur when there is a nomination of a custodian in a will or other instrument providing for the transfer of property on the occurrence of a future event. The new law provides that such instruments may name substitute custodians to whom the property must be transferred in the order named, if the first nominated custodian dies before the transfer or is unable, declines, or is ineligible to serve. Prob C §3903. Unfortunately, the statutory forms in Prob C §3909 do not provide for nomination of a substitute with the result that this precaution may be overlooked.

If no substitute is named, there may be problems depending on the type of instrument involved. If the omission occurs in a will or trust, the personal representative or trustee has the power to name the custodian under Prob C §3905(c). For life insurance, employee benefits, and P.O.D. accounts not exceeding $10,000, the obligor can name a member of the family as custodian under Prob C §3907. However, if a Prob C §3907 transfer exceeds $10,000, the statute is ambiguous. The CUTMA's general provision regarding substitute custodians is Prob C §3918(a). That provision appears to authorize the transferor to name the substitute. Unfortunately, the provision is inartfully worded, with the result that the statute appears to apply in cases of a declination to act, but not in cases of death or disability. Presumably, a court faced with the question would reach a more reasonable conclusion, but a clarifying amendment would be desirable. In the meantime, care should be taken to designate an adequate number of substitute custodians.

It should be noted that wills for clients with small estates should name substitute custodians rather than leaving the choice of a substitute to the executor. Under a conforming amendment to Prob C §630, a custodian may collect a small estate by affidavit. Stats 1984, ch 451. Effective January 1, 1985, the procedure will be available for estates not exceeding $60,000. Assuming a nominated but unappointed executor has no power to name a substitute custodian, leaving the selection of the substitute custodian to the executor would undoubtedly defeat the goal of avoiding formal court proceedings.

If a custodian ceases to act after he has assumed office, the problem becomes one of naming a successor custodian rather than a substitute. Former law allowed the original transferor to nominate successors in the original transfer document. CC §1161(a). Unfortunately, there is no comparable provision under CUTMA. Instead, the new law follows former CC §1161(b) by providing that the custodian nominates his successor. If the custodian dies or becomes incapacitated without making a nomination, a beneficiary who has attained the age of 14 may name an adult member of his family as custodian. Prob C §3918(d). If the beneficiary fails to act, his "conservator" becomes the custodian. A "conservator" in the terminology of the CUTMA is either a guardian of a minor or a conservator of an adult. If all else fails, the successor is appointed by the superior court.

G. Role of the Custodian

Probate Code §3911(b) vests custodianship property in the minor indefeasibly, but gives the custodian (and removes from the minor) all rights, power, duties, and

authority with respect to the property. Probate Code §3912 lists the custodian's duties as: (1) taking control of the property, (2) registering or recording title if necessary, and (3) managing and investing it. Under this section, a custodian is subject to a prudent person standard, altered now to refer to the care that a prudent person would observe when dealing with property of another, rather than his own property. The custodian, however, is also now authorized to retain property received from the transferor. Although the California statute omits language in the Uniform Act which would apply a higher standard to professional fiduciaries, our case law would appear to impose a higher standard. See *Estate of Beach* (1975) 15 C3d 623, 635, 125 CR 570, 577. Subject to the prudent person rule, Prob C §3913 grants extremely broad powers to the custodian. All powers previously specified in the code are gone and are replaced with simple language referring to all powers that a single adult would have over his or her own property.

The custodian must keep records of all transactions, including information necessary to prepare tax returns, and must make them available at reasonable intervals for inspection by a parent or legal representative or by the minor if the minor has attained the age of 14. Prob C §3912(e). Specified persons may require a court accounting under Prob C §3919. Presumably, the custodianship is not a separate tax entity (but see discussion below), so the minor's social security number must be used for accounts.

The custodian is authorized to "deliver or pay to the minor or expend for the minor's benefit as much of the custodial property as the custodian considers advisable for the use and benefit of the minor, without court order and without regard to (1) the duty or ability of the custodian personally, or any other person, to support the minor or (2) any other income or property of the minor which may be applicable or available for that purpose." Prob C §3914. The provision is intentionally broader and less definite than the "support, maintenance, education and benefit" standard of current law. CC §1158(b). The change avoids the implication that custodial property can be used only for the required support of the minor. National Conference of Commissioners on Uniform State Law, "Uniform Transfers to Minors Act," p 28. The comment to the Uniform Act also makes clear that the "use and benefit" standard permits the payment of the minor's legally enforceable obligations such as taxes and tort claims. If the custodian did not pay such obligations, a judgment creditor of the minor could levy on the custodial property.

H. Compensation of the Custodian

A custodian who is the donor of the custodial property or has appointed it by exercise of a power of appointment is not entitled to compensation for services as a custodian. In all other cases, the custodian has a noncumulative election during each calendar year to charge reasonable compensation for services performed during that year. Prob C §3915(b). The custodian is also entitled to reimbursement of reasonable expenses.

Compensation affects the custodian's risks. A custodian who is not compensated will be liable only for losses that result from bad faith, intentional wrongdoing, or gross negligence, even if the custodian has not observed the prudent person standard of Prob C §3912(b).

I. Liability of Custodian and Minor

Under Prob C §3917, a "claim based on (1) a contract entered into by a custodian acting in a custodial capacity, (2) an obligation arising from the ownership or control of custodial property, or (3) a tort committed during the custodianship" may be asserted against the custodian in the "custodial capacity." The custodian is not personally liable for a contract made as custodian unless the contract fails to disclose the custodial capacity. Unless there is personal fault, neither the custodian nor the beneficiary is personally liable for obligations arising from control of custodial property or for torts committed during the custodianship.

Analysis

A. Limitations of the Act

Despite the improvements over its predecessor, the CUTMA still imposes many limitations on custodianships. Some of the limitations are unavoidable; the goals of flexibility and protection of minors can conflict, and tax considerations further reduce the options. Other limitations may be cured by subsequent legislative action as California continues to improve the Act.

The present version of the statute provides that custodianships created by gift must terminate by age 21. Prob C §3920.5(e). The provision is designed to protect against loss of IRC §2503(c) tax benefits. However, those benefits are not always desired (*e.g.*, the annual exclusion has already been used or the transferor's wealth is too modest to create transfer tax concerns). It would be desirable to have a method for the transferor to make a knowing waiver of the statutory protection and select a higher termination age. This is not without precedent in the Act. Probate Code §3914(d), discussed below, currently provides a method for a transferor to elect an alternate set of distribution powers if the transferor is going to be the custodian and does not want the custodial property to be in his estate. The election is made by filing a document

with the superior court. Perhaps the same procedure could be used for those wanting to extend gift custodianships beyond age 21.

Another significant limitation of custodianships is the lack of any method for designating an alternate beneficiary. If the minor dies before receipt of the custodial property, it must be transferred to the minor's estate. This limitation may be inherent in the nature of custodianships, because a provision for an alternate beneficiary would conflict with the concept of the custodial property being vested in the minor.

Another drawback is the absence of any provision for co-custodians to serve at the same time. Co-trustees are often used for trusts where the two trustees serve different functions, such as those related to investments and those related to distribution decisions, or where a co-trustee with the grantor will prevent income being taxed to the grantor.

Nothing in the Act permits a custodian to settle or release a claim of a minor against a third party. The CUTMA provides that: "A written acknowledgment of delivery by a custodian constitutes a sufficient receipt and discharge for custodial property transferred to the custodian" (Prob C §3908), but the California Law Revision Commission comment makes clear that a release of a claim may only be made by a guardian, guardian ad litem, or other person expressly authorized by law to act for the minor. As a result, debtors of minors may be reluctant to make payment to a custodian.

Although Prob C §3910 permits multiple transfers to the same custodian for the same minor to be all part of one custodianship, and although Prob C §3918(b) allows a custodian to resign and appoint a successor other than a transferor, we may be unable to use these provisions to consolidate custodianships formed under the old and new law, because Prob C §3910 refers to custodial property held "under this part."

A custodianship does not include the safeguards of a spendthrift clause often found in trusts for minors. The California Law Revision Commission comment to Prob C §3914 expressly acknowledges that judgment creditors of the minor may levy on the custodianship.

B. Taxation

Uniform Gifts to Minors Act custodianships raised a number of tax questions, many of which were never firmly resolved. Despite the new law's attempt to address two of the major problem areas, ambiguities remain. It should be stressed at the outset that the tax issues are rather limited in scope and should not result in widespread avoidance of custodianships as an estate planning device. For example, we note below that there is a potential risk that the property of a custodianship will be included in the estate of the transferor if he is also the custodian. But this problem only affects a specific type of transfer, it is irrelevant for transferors with modest assets, and it can be solved by naming a different custodian.

1. Income tax. It is widely assumed that unless custodial income is used for the benefit of someone other than the minor, the minor will be treated as the owner of custodial property for tax purposes with the result that the income is taxed to the minor. This assumes that a custodianship will be treated for tax purposes as equivalent to a guardianship rather than characterized as a trust. This may assume too much. In *Anastasio v Commissioner* (1977) 67 TC 814, aff'd (2d Cir 1977) 573 F2d 1287, the Service contended that a custodianship should be taxed as a trust because the restrictions of custodianships preclude the beneficiary from possessing the attributes of ownership and enjoyment. The argument was rejected, but the Service has never acquiesced, and the argument that a custodianship is similar to a guardianship may be less convincing when the custodianship extends beyond the age of majority—particularly if it extends beyond age 21. Clarification of this point is needed. Characterizing a custodianship as a trust would not necessarily result in adverse tax consequences, but custodians would be required to file tax returns, and planning and distribution decisions would be affected.

Regardless of characterization, the new Act, like its predecessor, raises the issue of the effect of using custodial income for the minor's benefit. In 1956, the Service ruled that regardless of the relationship of the donor or custodian to the donee, income derived from property held in a custodianship under the Model Gifts of Securities to Minors Act, "which is used in the discharge or satisfaction, in whole or in part, of a legal obligation of any person to support or maintain a minor is, to the extent so used, taxable to such person under section 61 of the Internal Revenue Code of 1954." Rev Rul 56-484, 1956-2 Cum Bull 23, 24.

Perhaps not coincidentally, that was the same year that the Service adopted regulations for the grantor trust rules (IRC §§671-679). The grantor trust rules tax to the grantor any trust income which is actually used to support or maintain a person the grantor is legally obligated to support. Also, a trustee or power holder who is not the grantor but who has a fiduciary power exercisable solely by himself to apply trust income to maintain persons he is obligated to support will be taxed on the trust income so applied. It may well be that the Service issued Rev Rul 56-484 for the purpose of serving notice that it would not permit custodianships to be used to obtain better tax results than could be achieved with trusts. In 1959, the Service reached the same conclusion for custodianships

under the Model Uniform Gifts to Minors Act. Rev Rul 59-357, 1959-2 Cum Bull 212.

The CUTMA follows the Uniform Act in attempting to circumvent these rulings by providing that a delivery, payment, or expenditure to the minor or for his benefit is "in addition to, not in substitution for, and does not affect any obligation of a person to support the minor." Prob C §3914(c). This is apparently an attempt to declare that the payment is not to benefit the person having the legal obligation of support. Whether the statute will actually avoid attribution of the income in a case where custodianship funds are in fact used to provide support owed to the minor by another is less certain.

It should be noted that the California Law Revision Commission comment substantially repeats the comment to the Uniform Act. Both include a reference to Reg §1.662(a)-4, which provides that there is a legal obligation to support another person for purposes of attribution of trust income "if, and only if, the obligation is not affected by the adequacy of the dependent's own resources." The purpose of making this reference is unclear and confusing. The regulation itself is understandable in relation to a person's duty to support indigent parents, for example, but it it appears that in California (and elsewhere) a "parent possessing adequate financial resources has a duty to provide his or her child with basic support regardless of the child's independent resources." *Armstrong v Armstrong* (1976) 15 C3d 942, 949, 126 CR 805, 809. Further, as noted above, it is not at all clear that provisions related to the taxation of trusts have any application to custodianships.

On balance, it is reasonable to assume that the Service will continue to attempt to attribute to parents any custodial income actually used to support a minor. However, it is also possible, if that use is clearly a breach of fiduciary duty, that the parties' rights, not their conduct, will control for this purpose. Of course, if the parents are already fully meeting their support obligations, additional payments by the custodian would not be in discharge of those obligations. For a discussion of the extent of the support obligation for purposes of the grantor trust rules, see the discussion of *Frederick C. Braun, Jr.* (1984) 48 CCH TCM 210, P-H TCM ¶84,285, at 6 CEB Est Plan R 15 (1984).

2. Estate tax. The new Act does not alter the estate tax problems of its predecessor. If a gift would otherwise remove property from the transferor's estate, the result is normally not changed by the fact that the gift is made to a custodian unless the transferor names himself as custodian. If, however, the transferor appoints himself custodian and dies while serving in that capacity, his extensive powers over the property may cause it to be included in his estate under IRC §2038; and if the minor is also a dependent of the transferor, his power to use the fund to discharge his obligation of support may cause inclusion under IRC §2036. See *Estate of Jack F. Chrysler* (1965) 44 TC 55, rev'd because of other facts of particular case (5th Cir 1966) 361 F2d 508.

Immediately following *Chrysler*, California attempted to solve this problem by enactment of CC §1158.5. See Review of Selected 1965 Code Legislation 52-53 (Cal CEB 1965). This provision, now incorporated in new Prob C §3914(d), provides that a transferor-custodian can elect to have his powers governed by that special provision, in which case the custodian cannot make any distributions to or for the minor except by order of the court on a showing that the expenditure is necessary for the support, maintenance, or education of the minor. The election is made in writing and must be filed with the superior court. Whether the statute accomplishes its purpose apparently has never been determined by the courts. It probably solves problems under IRC §§2038 and 2036(a)(2), but may not solve problems under IRC §2036(a)(1), and also §2041.

Even greater uncertainty is involved if the custodial property is insurance on the life of the custodian. In addition to the problems with IRC §§2036 and 2038, the power of the custodian to do such things as change the form of the benefit or surrender the policy may result in inclusion in the custodian's estate under IRC §2042(2). It may be possible to avoid this result by causing the policy to be issued without any power in the insured to do anything other than pay the premiums. Some carriers will now issue policies in this fashion.

Conclusion

Despite the tax problems and various areas of potential improvement, the CUTMA should now serve the needs of many people as a simple form of transfer without the attendant expense of a trust or guardianship. It has great breadth as to when transfers may be made and what types of property may be used. It allows custody to continue until an age more in accord with the desires of clients. It may be a convenient solution for a contingent distribution in a will to grandchildren, as it will not unduly lengthen the instrument, and may be more readily understandable and less expensive to draft. In other words, it is now time to reconsider the reluctance of attorneys to use this Act, review its new provisons, and include it as a valuable tool in the estate planner's bag of tricks.

Memo 85-16 EXHIBIT 2

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October 12, 1984

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Re: Uniform Transfers to Minors Act

Dear Mr. De Moully:

I have been assisting Mr. Jeffrey Dennis-Strathmeyer in the preparation of an article for a forthcoming CEB newsletter on the new Uniform Transfers to Minors Act.

Although there are several minor changes that could be considered for better tax results, the act in substance is an outstanding job. I would like to call to your attention, however, one very important point that may have been overlooked by reason of the fact that it is not part of the Uniform laws.

Prior California law under CC §1161(a) allowed a donor to designate successor custodians. This section appeared to apply whether or not the initially named custodian actually first took possession of the property.

The new act does not carry this section, and the only thing a donor can do now is to nominate a successor if no one has ever taken the possession of the custodial property.

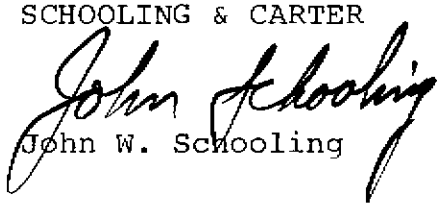
This is a deletion of a very valuable point contained in prior California law, it was not discussed as an intentional deletion in any of your materials, and I doubt that there is any rationalization for it. I suspect that the only reason it was omitted is that it was overlooked. It is not part of the Uniform Act.

It is actually my recommendation that the law revision commission consider a further enlargement to this area. It would be my opinion that co-custodians should be permitted. Co-trustees are commonly appointed, as in many situations there are valuable aspects of having more than one person involved. Having a co-custodian would, of course, also serve to eliminate any hiatus that might be caused by the death of one of the custodians since the survivor would still remain as a custodian.

Thank you for your consideration of these matters.

Very truly yours,

PETERS, FULLER, RUSH,
SCHOOLING & CARTER



John W. Schooling

JWS:bb

cc: Jeffrey A. Dennis-Strathmeyer
Ed Halbach, Jr.

EXHIBIT 3

1161. (a) A donor may, in the same transaction and by the same document by which the gift is made, designate one or more successor custodians to serve, in the designated order of priority, in the event that the custodian originally named or a prior successor custodian shall be unable to act as custodian, decline to accept the custodianship, resign, die, or become legally incapacitated by setting forth the successor custodian's name, followed in substance by the words: "is designated [first, second, etc., where applicable] successor custodian."

3918. (a) A person nominated under Section 3903 or designated under Section 3909 as custodian may decline to serve by delivering a valid disclaimer under Division 2.5 (commencing with Section 260) to the person who made the nomination or to the transferor or the transferor's legal representative. If the event giving rise to a transfer has not occurred and no substitute custodian able, willing, and eligible to serve was nominated under Section 3903, the person who made the nomination may nominate a substitute custodian under Section 3903; otherwise the transferor or the transferor's legal representative shall designate a substitute custodian at the time of the transfer, in either case from among the persons eligible to serve as custodian for that kind of property under subdivision (a) of Section 3909. The custodian so designated has the rights of a successor custodian.

(b) A custodian at any time may designate a trust company or an adult other than a transferor under Section 3904 as successor custodian by executing and dating an instrument of designation before a subscribing witness other than the successor. If the instrument of designation does not contain or is not accompanied by the resignation of the custodian, the designation of the successor does not take effect until the custodian resigns, dies, becomes incapacitated, or is removed. **The transferor may designate one or more persons as successor custodians to serve, in the designated order of priority, in case the custodian originally designated or a prior successor custodian is unable, declines, or is ineligible to serve or resigns, dies, becomes incapacitated, or is removed. The designation either (1) shall be made in the same transaction and by the same document by which the transfer is made or (2) shall be made by executing and dating a separate instrument of designation before a subscribing witness other than a successor as a part of the same transaction and contemporaneously with the execution of the document by which the transfer is made. The designation is made by setting forth the successor custodian's name, followed in substance by the words: "is designated [first, second, etc., where applicable] successor custodian." A successor custodian designated by the transferor may be a trust company or an adult other than a transferor under Section 3904. A successor custodian effectively designated by the transferor has priority over a successor custodian designated by a custodian.**

(c) A custodian may resign at any time by delivering written notice to the minor if the minor has attained the age of 14 years and to the successor custodian and by delivering the custodial property to the successor custodian.

(d) If the transferor has not effectively designated a successor custodian, and a custodian is ineligible, dies, or becomes incapacitated without having effectively designated a successor, and the minor has attained the age of 14 years, the minor may designate as successor custodian, in the manner prescribed in subdivision (b), an adult member of the minor's family, a conservator of the minor, or a trust company. If the minor has not attained the age of 14 years or fails to act within 60 days after the ineligiblity, death, or incapacity, the conservator of the minor becomes successor custodian. If the minor has no conservator or the conservator declines to act, the transferor, the legal representative of the transferor or of the custodian, an adult member of the minor's family, or any other interested person may petition the court to designate a successor custodian.

(e) A custodian who declines to serve under subdivision (a) or resigns under subdivision (c), or the legal representative of a deceased or incapacitated custodian, as soon as practicable, shall put the custodial property and records in the possession and control of the successor custodian. The successor custodian by action may enforce the obligation to deliver custodial property and records and becomes responsible for each item as received.

(f) A transferor, the legal representative of a transferor, an adult member of the minor's family, a guardian of the person of the minor, the conservator of the minor, or the minor if the minor has attained the age of 14 years, may petition the court to remove the custodian for cause and to designate a successor custodian other than a transferor under Section 3904 or to require the custodian to give appropriate bond.

(g) Upon the filing of a petition under subdivision (d) or (f), the court shall grant an order, directed to the persons and returnable on such notice as the court may require, to show cause why the relief prayed for in the petition should not be granted and, in due course, grant such relief as the court finds to be in the best interests of the minor.