

Memorandum 85-21

Subject: Study L-640 - Trusts (Proof of Oral Trusts)

At the September 1984 meeting the Commission decided to codify the existing law requiring proof of oral trusts in personal property by clear and convincing evidence. The staff suggestion to make oral trusts unenforceable was rejected. Professor Russell D. Niles, a Commission consultant, has written a short memorandum that suggests a refinement of the rule governing proof of oral trusts. You should read his memorandum, which is attached hereto as Exhibit 1.

Professor Niles suggests adoption of a statute modeled after the Texas statute which is set out on page 2 of his memorandum. The gist of the suggested change is that a writing should be required to approve an oral trust where the owner does not transfer the property to another person. Professor Niles is especially concerned with the situation where, after the death of the owner, a person claims that the deceased owner held the property on an oral trust for the claimant's benefit. In this case, under California law, it appears that clear and convincing evidence of an oral declaration of trust would suffice to uphold the trust.

Professor Niles also notes that in an analogous situation Probate Code Section 150, enacted on recommendation of the Commission, requires written evidence of a contract to make a will. (See Exhibit 1, p. 5.) As for oral trusts, Professor Niles suggests that earmarking property might be sufficient to uphold the trust.

The Commission should consider adopting a rule that some objective evidence of an intent to create a trust is required before an oral trust in personal property may be enforced after the death of the owner. Such evidence would include a writing or earmarking; the terms of the trust would not need to be written.

The Commission should also consider whether some objective evidence of the intent to create a trust should be required of oral trusts in personal property during the lifetime of the owner. From the point of

view of a creditor of the property owner, there should be some objective evidence of the donative transfer in trust, even if only a contemporaneous earmarking of the trust property.

A discussion draft of a section to accomplish these purposes is attached hereto as Exhibit 2.

Respectfully submitted,

Stan G. Ulrich
Staff Counsel

EXHIBIT 1

MEMORANDUM

To : California Law Revision Commission

From: Russell D. Niles

Re : Oral Trusts Memorandum 84-24 and Supplements

Date: October 25, 1984

The staff has recommended that the Commission propose an amendment to the California Statute of Frauds along the lines of the recent amendment of the Indiana Code. The Indiana statute reads as follows:

30-4-2-1- Formal requirements

Sec. 1. (Formal requirements)

(a) A trust in either real or personal property is enforceable only if there is written evidence of its terms bearing the signature of the settlor or his authorized agent.

(b) Except as required in the applicable probate law for the execution of wills, no formal language is required to create a trust, but its terms must be sufficiently definite so that the trust property, the identity of the trustee, the nature of the trustee's interest, the identity

of the beneficiary, the nature of the beneficiary's interest, and the purpose of the trust may be ascertained with reasonable certainty.

If the Commission should not approve the Indiana statute, the staff recommends the Texas statute, which reads as follows:

Section 112.004. STATUTE OF FRAUDS. A trust in either real or personal property is enforceable only if there is written evidence of the trust's terms bearing the signature of the settlor or the settlor's authorized agent. A trust consisting of personal property, however, is enforceable if created by:

(1) a transfer of the trust property to a trustee who is neither settlor nor beneficiary if the transferor expresses simultaneously with or prior to the transfer the intention to create a trust, or

(2) a declaration in writing by the owner of the property that the owner holds the property as trustee for another person or for the owner and another person as a beneficiary.

Professor Dukeminier has opposed change in the existing California law which now permits the enforcement of oral express trusts of ~~personal~~ property if the proof is clear.

He points out that the requirement of written evidence of the terms of a trust would require the expansion of the law of constructive trust to avoid unjust enrichment.

The letters of Professor Dukeminier to the Commission are persuasive in the common cases where personal property is delivered by an owner to another person as trustee for a third person or where the owner conveys or devises personal property to another on the latter's oral agreement to hold in trust. If relief is not available under the law of oral express trusts, then relief will generally be available under the doctrine of constructive trust. Professor Dukeminier has also suggested that there is not much advantage in establishing a trust one way or the other. The delivery, the conveyance or the will indicate that the owner had a final intention to confer a benefit.

I agree with professor Dukeminier that we should use great caution in changing existing law unless there is clear reason for doing so. I do not think there is sufficient reason to accept the Indiana statute. I suggest, however, that there is good reason to consider the more limited change involved in the Texas statute.

Section 112.004 in subsection (1) does not attempt to change traditional law where the owner has made a legal transfer of the trust property to another person and there

is an intent to create a trust. Although the language of the statute is somewhat cryptic, the statute leaves untouched the oral trusts that would usually be held to be constructive trusts to avoid unjust enrichment. What is new and contrary to the present California law is that subsection (2) requires a writing where the owner makes no transfer to another person.

The express trust created by an owner by an oral declaration without delivery or any writing or other objective confirmation of the creation of the trust is dangerous in several particulars. In the first place, the owner is in a position to defraud creditors and others while alive, and secondly, after the death of the donor, there is temptation for family conflicts and litigation.

The case that persuaded the Indiana Commission to recommend a tightening up on the Statute of Frauds was Hinds v. McNair [235 Ind. 34, 129 N.E.2d 553 (1955)]. A judgment creditor of a parent sought to levy on stock which had been issued to the parent in his name. The parent claimed that he held the stock as trustee of an oral trust for his children. There was no proof of the trust except the unsupported evidence of the parent. The trial court had believed him and the appellate court could not hold as a matter of law that the trial court erred.

It is ^{the} post mortem aspect of the rule that concerns me even more. I think it is very dangerous after the death of an owner to have a donee claim that the owner held on an oral trust, even if the standard of proof is high.

Under the present California law evidence of an oral declaration alone, if clear and convincing, would suffice. And in these cases the property involved might be more than an India bond, it might involve half of the decedent's estate. Under the Texas statute, without a transfer to another person (by delivery, conveyance, or will) under subdivision (1) or a writing under subdivision (2) the trust could not be proved.

The Commission has already considered the analogous problem of the proof of oral contracts to make or not to revoke a will. Under the new §150 of the Probate Code [added by Stats. 1983, C. 842, §22, applicable after December 31, 1984] the law provides that a contract to make a will or devise, or not to revoke a will or devise, or to die "intestate", can be established only by one of the following: "1) Provisions of a will stating material provision of the contract. 2) An express reference in a will to a contract and extrinsic evidence proving the terms of the contract. 3) A writing signed by the decedent evidencing the contract."

Under the Texas statute, the writing need not be a complete trust instrument: the declaration need not include the terms of the trust. [Commentary to §102.004. Statute of Frauds, ^{re} printed in Exhibit 1 of Memorandum 84-25.] So, in Probate Code §150 there must be something in writing. Evidence of oral statements alone are not sufficient.

Professor Dukeminier believes that oral trusts declared by an owner should be permitted because they offer an opportunity for the courts to carry out the intention of an owner by the fiction of a trust to avoid the requirement of delivery. He approves the thesis of Professor Sarajane Love in her recent article, "Imperfect Gifts as Declarations of Trusts, An Unapologetic Anomaly" [67 KY. L.J. 309 (1978)]. I stand with Professor Scott in upholding the later English cases (cited by Professor Love) which refused to save inchoate or imperfect gifts by construing them to be oral express trusts.

It might be that the Texas statute could be improved. Perhaps subdivision (2) could be somewhat expanded so that an owner could create a trust of personal property by oral declarations if the owner thereafter earmarked the property (by a deposit of money in trust name, by a registration of a bond in trust name, by the issuance of stock in trust name,

or by the owner rendering an account to a beneficiary in writing). But an oral declaration of a trust by an owner to a grandchild, a church, a college, a nurse or a cohabitor--without more--could be a litigation breeder. These cases may not be frequent considering the present high threshold of proof, but they could involve a very substantial fraction of a donor's estate after death. A few successful claims could invite a flood.

I urge the staff to attempt a redraft of the Texas statute. Even Professor Dukeminier has conceded that after the death of the owner, oral trusts are not likely to be enforced unless there is objective evidence of an intent to create a trust.

EXHIBIT 2

Staff Draft§ 607. Oral trusts of personal property

607. (a) The existence and terms of an oral trust of personal property may be established only by clear and convincing evidence.

[(b) The oral declaration of the trustor is not sufficient evidence of creation of the trust unless trust property was transferred, actually or constructively, at the time of the declaration or thereafter.]

(c) A reference in this division or elsewhere to a trust instrument means in the case of an oral trust the terms of the trust as established pursuant to subdivision (a).

Comment. Subdivision (a) of Section 607 codifies the rule requiring clear and convincing evidence of creation of an oral trust in personal property. See, e.g., *Lefrooth v. Prentice*, 202 Cal. 215, 227, 259 P. 947 (1927); *Kobida v. Hinkelmann*, 53 Cal. App.2d 186, 188-93, 127 P.2d 657 (1942); *Monell v. College of Physicians & Surgeons*, 198 Cal. App.2d 38, 48, 17 Cal. Rptr. 744 (1961). Under this rule circumstantial evidence is not sufficient. See *Fahrney v. Wilson*, 180 Cal. App.2d 694, 696, 4 Cal. Rptr. 670 (1960).

[Subdivision (b) provides a new requirement for the validity of oral trusts. Under subdivision (b), a delivery of personal property to another person accompanied by an oral declaration by the transferor that the transferee holds it in trust for a beneficiary creates a valid oral trust. Constructive delivery, such as by earmarking property or recording it in the name of the transferee, is also sufficient to comply with subdivision (b).]

Subdivision (c) is intended to facilitate application of trust statutes to properly established oral trusts. By operation of this section, an oral trust may be shown to be irrevocable even though Section 640 provides that a trust is revocable unless it is made expressly irrevocable by the instrument creating the trust.

Nothing in this section affects the law concerning constructive trusts. See Section 504. Hence, in appropriate circumstances, an attempted disposition of property that fails to satisfy the requirements for an oral trust under Section 607 may be remedied through the mechanism of a constructive trust.

Note. Subdivisions (a) and (c) implement Commission decisions made at the September 1984 meeting.