#L-3013

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Second Supplement to Memorandum 90-22

Subject: Study L-3013 - Uniform Statutory Rule Against Perpetuities (Articles received from Professors Fellows and Waterbury)

The staff has just received draft versions of two law review articles concerning the Uniform Statutory Rule Against Perpetuities. We have decided not to reproduce all 194 pages of this material, but instead have attached the conclusions of the two articles.

Professor Mary Louise Fellows has analyzed how perpetuities cases would be decided under USRAP in her article, *Testing Perpetuity Reforms: A Study of Perpetuity Cases 1984-89*. (See Abstract, in Exhibit 1.) Professor Fellows concludes that the deferred *cy pres* scheme in USRAP would be no more difficult, and perhaps would be easier, to administer than the immediate *cy pres* scheme such as that in existing California law.

Professor Thomas Waterbury argues that choice of law rules permit creation of perpetual trusts of personal property (since three states have no Rule Against Perpetuities) in his article *Some Choice of Law Aspects of Perpetuities Reform*. (See Summary and Conclusions, in Exhibit 2.) Consequently, Professor Waterbury believes that the traditional rule will typically victimize the drafter of a local trust that attempts to comply with it, whereas sophisticated estate planners will be able to ignore the rule. Professor Waterbury concludes that the 90-year wait-and-see rule of USRAP would encourage perpetual trusts that would spend their first 90 years in the local jurisdiction and then move to a state without any Rule. He believes under these conditions that abolition of the Rule is acceptable and that immediate *cy pres* (as in California) is preferable to USRAP.

Respectfully submitted,

Stan Ulrich
Staff Counsel

EXHIBIT 1

Abstract of

Fellows, *Testing Perpetuity Reforms: A Study of Perpetuity Cases 1984-89* (1990)

ABSTRACT

This article subjects the USRAP to the empirical test of determining how it would perform if it had applied in the sixteen perpetuity cases reported during the last five years. Analysis of the 1984-89 cases shows that the USRAP's deferred perpetuity reformation approach minimizes perpetuity litigation and minimizes the risk of judicial error by postponing judicial intervention until the time when more information about family circumstances is known. The analysis also demonstrates that fashioning a remedy at the end of the perpetuity period is no more difficult, and perhaps easier, than fashioning it at the beginning.

The review of the cases further shows that the USRAP's perpetuity rule, which relies on a life-in-being measuring rod through its common-law Rule branch and a ninety-year measuring rod through its wait-and-see branch, avoids unwarranted interference with a transferor's estate plan while guaranteeing that a trust does not last too long. The case analysis demonstrates that generally the choice of measuring rods is irrelevant because the trusts will terminate well within either a ninety-year or a life-in-being perpetuity period. Even if remote contingencies occur preventing interests from vesting or terminating within a state's perpetuity period, the case analysis shows that the different measuring rods generally produce perpetuity periods of about the same length. Only in the unusual family situations in which adult children who had not yet had their own children, did the ninety-year rule result in a substantially longer perpetuity period. Even if the ninety-year rule allows the trusts in these cases to last "too long" according to conventional wisdom, the article shows why that is a small cost to pay for the advantage of administrative simplicity obtained by the ninety-year rule. The article further shows, through history and logic, why a perpetuity law that relies exclusively on the life-in-being measuring rod is unsatisfactory.

In sum, the case analysis demonstrates that the widespread endorsements of the USRAP, along with its exceptional reception in state legislatures, are well deserved. It provides a perpetuity law that efficiently and effectively achieves a fair balance between present and future property owners.

EXHIBIT 2

Summary from draft of
Waterbury, *Some Choice of Law Aspects of Perpetuitites Reform*
(Feb. 8, 1990)

III.

Summary and Conclusions

Most states have rules against perpetuities, Gray's Rule or some statutory mutation of it, which indirectly limit the permissible duration of private trusts to about a century. Three states, however, do not restrict the permissible duration of such trusts. Ordinarily, family trusts are designed to endure for much less than a century. Few contemporary settlors wish to create trusts likely to last that long. Moreover, a settlor who wishes to create a potentially perpetual family trust can avoid any domiciliary rule against perpetuities by creating an inter vivos trust of personalty in one of the three permissive states.

The question arises, therefore, whether these numerous state rules against perpetuities accomplish enough to merit retention.

At the policy level, the case for retention is limited by the permissiveness of a century long perpetuities period. Thus the economic policy case against transfers that render specific assets inalienable is a case for rules assuring their alienability within a much shorter period of time. Essentially, retention must be defended on grounds of social policy. Eminent authorities support the view that the essential function of rules against perpetuities is to permit "succeeding generations" to be free to dispose of family property. Since few settlors wish to continue trusts beyond a century, and since few Americans will benefit from a long-term family trust in any case, the social importance of this function is surely limited. The writer is fonder of the converse argument that private trusts shield beneficiaries from the burdens of property management, and that a century of such protection is quite sufficient; this seems, however, to be an isolated view. Other arguments for rules against perpetuities, when examined, seem less persuasive. At the policy level, therefore, it is not clear that American society has benefited much from state rules against perpetuities.

At the technical level, the fact that some states permit potentially perpetual private trusts compromises the effectiveness of <u>any</u> state rule against perpetuities. Under settled choice of law doctrine, a settlor domiciled in State X,

where Gray's Rule is in force, is free to establish a potentially perpetual inter vivos trust of personalty in State Y, which permits such trusts, despite the fact that the settlor and trust beneficiaries are State Y residents. Thus State X cannot enforce the policy of Gray's Rule against its intended target - well-planned potentially perpetual private trusts. Instead, the usual victim of Gray's Rule will be an ordinary local trust that conforms to its policy, but is technically defective. These facts create a solid case for abolishing Gray's Rule, persuasive to those uncommitted to its social importance.

Those hostile to potentially perpetual private trusts, however, will resist abolition because, at least, Gray's Rule prevents the deliberate creation of such a trust for administration within the state.

One alternative to abolition is the USR, a Uniform Act stemming from the American Law Institute's revision of Gray's Rule[143]. The USR seeks to enforce the policy of Gray's Rule without burdening ordinary trusts. The chosen vehicle, a 90 year wait-and-see provision, allows non-vested interests that might vest within 90 years to endure for that period. Thereafter, vesting is enforceable by reformation.

The amnesty provided by the 90 year wait-and-see period promises to shield ordinary trusts from reformation - because they will terminate within that period. The same 90 year period, however, compromises the policy of Gray's Rule. Under trust law, powers to remove and replace trustees may be employed to shift

the situs of a trust's administration from one state to another. Under choice of law doctrine, a settlor may provide that governing law, including that governing the validity of the trust, may change to that of a new situs of administration. Thus a potentially perpetual private trust may be initially established in a USR state, and, protected against an interim adjudication of invalidity by the 90 year wait-and-see period, be moved to a state permitting such trusts before the 90 year period expires. Having arrived, the trust will be valid at its new situs of administration. This possibility may well be attractive to informed settlors, estate planners, and professional fiduciaries, in a USR state. Accordingly, given even one state which permits potentially perpetual private trusts, as Wisconsin has done since 1902, the USR invites local creation and administration of such trusts for up to 90 years.

Viewed then as an alternative to abolition, the USR essentially offers a more tactful route. It does, however, bar potentially perpetual trusts of local land.

Opponents of abolition should, instead, focus on the alternative of an immediate reformation statute. An immediate reformation statute has been in force in California for a generation, and has also been in force for some years in three other states. Such statutes modify Gray's Rule by requiring immediate reformation of interests that might vest remotely. This remedy is much less harsh than invalidating such interests, the penalty imposed by Gray's Rule. It does require legal

proceedings to achieve reformation, but transfers requiring reformation are uncommon. Also, the need for reformation will be minimized by a statute that directs reformation departing as little as possible from the settlor's original dispositions. Commonly, only the addition of a saving clause unlikely, in fact, to modify those dispositions will be required to assure vesting within the perpetuities period.

The writer's personal view is rather equivocal. Though the social importance of Gray's Rule is debateable, if no state permitted potentially [perpetual]* private trusts, he would not propose abolition in the first. That state of affairs, however, has not obtained since 1902. Currently, the writer's home state of Minnesota is bounded East and West by Wisconsin and South Dakota which have abolished Gray's Rule. It is also bounded on the South by Iowa, where an earlier equivalent of the USR is in force.[144] In this setting, abolition of Gray's Rule is a reasonable choice. And an immediate reformation statute is a reasonable alternative to abolition. It would minimize the impact of Gray's Rule on ordinary trusts, and bars local creation and administration of potentially perpetual private trusts. The USR, in contrast, is unattractive to the writer, offering too little matter with too much art.

* added by CLRC staff.