Study L-605 July 14, 2000

First Supplement to Memorandum 2000-50

Rules of Construction for Trusts (Comments of Jim Deeringer)

Attached as an Exhibit is a letter from Jim Deeringer, who has reviewed Professor McGovern's study on behalf of the Executive Committee of the Estate Planning, Trust, and Probate Law Section of the State Bar. Mr. Deeringer's comments are summarized below.

Prob. Code § 21102. Intention of transferor; rules of construction apply unless instrument indicates contrary intention

Professor McGovern proposes to revise this section as follows:

> 21102. (a) The intention of the transferor ~~as expressed in the instrument~~ controls the legal effect of the dispositions made in the instrument.
>
> (b) The rules of construction expressed in this part apply ~~where the intention of the transferor is not indicated by the instrument~~ in the absence of a finding of contrary intent by the transferor.

The staff agrees with the proposed amendment of subdivision (b) but not of subdivision (a). Mr. Deeringer takes the opposite position — he agrees with the proposed amendment of subdivision (a) but not of subdivision (b). He suggests the following emendation of Professor McGovern's rewrite of subdivision (b):

> (b) The rules of construction expressed in this part apply in the absence of ~~a~~ an express statement of intent in the instrument or a court finding of contrary intent ~~by~~ on the part of the transferor.

"This wording would allow extrinsic evidence to override the rules of construction but not express statements of intent, which is, I believe, the result we want." Exhibit pp. 1-2.

Prob. Code § 21104. "Testamentary gift" defined

Mr. Deeringer notes the anomalous use of the term "testamentary" gift to include a nontestamentary (nonprobate) transfer. He would at least make that usage more explicit in the statute.

21104. As used in this part, "testamentary gift" means a transfer in possession or enjoyment, including a nonprobate transfer, that takes effect at or after death.

Mr. Deeringer would actually prefer to replace the term "testamentary gift" with a more appropriate term, such as "at-death transfer". (This is a term frequently used by attorneys and other estate planning professionals in the tax planning context.)

21104. As used in this part, ~~"testamentary gift"~~ "at-death transfer" means a transfer in possession or enjoyment that takes effect at or after death.

Mr. Deeringer notes that this term is not completely satisfactory either, since it may imply that only transfers of present interests and not future interests are covered. But it is preferable to "testamentary gift".

Prob. Code § 21110. Anti-lapse

Express Requirement of Survival

Professor McGovern recommends that words of survival in an instrument should be subject to extrinsic evidence of the donor's intent:

...

~~(b)~~ (c) The issue of a deceased ~~transferee~~ beneficiary do not take in the ~~transferee's~~ beneficiary's place if the ~~instrument expresses~~ transferor expressed a contrary intention ~~or a substitute disposition. A requirement that the initial transferee survive for a specified period of time after the death of the transferor constitutes a contrary intention. A requirement that the initial transferee survive until a future time that is related to the probate of the transferor's will or administration of the estate of the transferor constitutes a contrary intention~~. With respect to multiple beneficiaries or a class of beneficiaries, a contrary intention is not expressed by a devise to the "surviving" beneficiaries or to "the survivor or survivors" of them, or words of similar import, in the absence of additional evidence.

Mr. Deeringer reports that the State Bar Executive Committee overwhelmingly favors retaining existing California law on this point — namely, that an express requirement of survival indicates an intention that the anti-lapse rule not apply (at least to the extent that the instrument in question is lawyer-prepared). It is the Committee's experience that lawyers use language of survival

purposefully to express the donor's actual intent. "Words of survivorship, *without more*, do not, in our experience, imply an intent to benefit the issue of a predeceased transferee." Exhibit, p. 3. Mr. Deeringer states that a change in the anti-lapse rule, particularly if applied retroactively, would create a great many administration problems and require the sale of tangible personal property in many cases where no such sale was contemplated by the transferor.

Mr. Deeringer notes that this concern relates primarily to attorney-drafted language of survival. However, he thinks that an effort to distinguish between attorney-drafted instruments and others would be difficult to effectuate, and a uniform rule that gives effect to survival language is probably preferable.

Application of Anti-Lapse Statute to Future Interests

Mr. Deeringer agrees with Professor McGovern's position on vesting of future interests, and suggests a few minor changes in wording:

> 21110. (a) As used in this section:
>
> (1) "Beneficiary" means a beneficiary who is kindred of the transferor or kindred of a surviving, deceased, or former spouse of the transferor.
>
> (2) A beneficiary under a class gift is a beneficiary unless the beneficiary's death occurred before the execution of the instrument ~~of transfer~~ and that fact was known to the transferor when the instrument ~~of transfer~~ was executed.
>
> (b) Subject to subdivision (c), (1) if a beneficiary of ~~a~~ ~~testamentary gift~~ at-death transfer is dead when the instrument ~~of transfer~~ is executed, or is treated as if the beneficiary predeceased the transferor, or fails to survive the transferor or (2) if the beneficiary of a future interest in any gift fails to survive until a future time required by the instrument ~~of transfer~~ (as interpreted by the preceding section), the issue of the deceased beneficiary shall take in the beneficiary's place in the manner provided in Section 240.
>
> ...

Prob. Code § 21116. Vesting of testamentary disposition

Mr. Deeringer questions Professor McGovern's suggested repeal of Section 21116. While the provision is inappropriately applied to future interests, it may be useful as applied to present interests. "In the administration of decedent's estates and trusts, it is helpful to have authority for the proposition that a beneficiary of a present interest is the *owner* of that interest as of the moment of death, subject only to administration of the estate or trust." Exhibit p. 4.

Mr. Deeringer floats a possible revision along these lines:

> 21116. ~~A testamentary disposition by an instrument, including a transfer to a person on attaining majority,~~ An at-death transfer of a present interest is presumed to vest at the transferor's death.

He concludes, however that as so revised the principle seems self-evident; Professor McGovern is probably correct that we do not need the section at all.

Prob. Code § 21120. Every expression given some effect; intestacy avoided

Professor McGovern notes the application of Section 21120 primarily to wills, but recommends no change in this section. Mr. Deeringer thinks it would be helpful to keep the provision and write it so that the principle applies to transfers by trust as well as by will:

> 21120. The words of an instrument are to receive an interpretation that will give every expression some effect, rather than one that will render any of the expressions inoperative. Preference is to be given to an interpretation of an instrument that will prevent ~~intestacy~~ failure of a transfer, rather than one that will result in ~~an intestacy~~ failure of a transfer.

Prob. Code § 21133. Unpaid proceeds of sale, condemnation, or insurance; property obtained as a result of foreclosure

Prob. Code § 21134. Sale by conservator; payment of proceeds of specifically devised property to conservator

Professor McGovern would repeal Sections 21133 and 21134 on the basis that California case law on ademption is adequate; the provisions do not serve a useful purpose.

Mr. Deeringer agrees with the premise, but not the conclusion — "The virtue of specific statutes such as §§ 21133 and 21134 is that they foreclose litigation (and even the necessity of uncontested petitions for orders determining entitlement to distribution) by leaving no doubt as to the proper result in such cases." Exhibit p. 5. Unless the California courts have unambiguously and uniformly ruled on each of the questions presented in the sections, he would not repeal them.

> 21133. A recipient of a specific gift has the right to the remaining property specifically given and all of the following:

(a) Any balance of the purchase price (together with any security interest) owing from a purchaser to the transferor at death by reason of sale of the property.

(b) Any amount of an eminent domain award for the taking of the property unpaid at death.

(c) Any proceeds unpaid at death on fire or casualty insurance on the property.

(d) Property owned by the transferor at death as a result of foreclosure, or obtained in lieu of foreclosure, of the security for a specifically given obligation.

21134. (a) Except as otherwise provided in this section, if specifically given property is sold by a conservator, the beneficiary of the specific gift has the right to a general pecuniary gift equal to the net sale price of the property.

(b) Except as otherwise provided in this section, if an eminent domain award for the taking of specifically given property is paid to a conservator, or if the proceeds on fire or casualty insurance on specifically gifted property are paid to a conservator, the recipient of the specific gift has the right to a general pecuniary gift equal to the eminent domain award or the insurance proceeds.

(c) This section does not apply if, after the sale, condemnation, fire, or casualty, the conservatorship is terminated and the transferor survives the termination by one year.

(d) The right of the beneficiary of the specific gift under this section shall be reduced by any right the beneficiary has under Section 21133.

Prob. Code § 21135. Ademption by satisfaction

Professor McGovern would repeal the Section 21135 rule on advancements as unnecessary and imposing an obstacle to ascertaining intent. Mr. Deeringer would not want to see the provision repealed — the premature satisfaction problem arises frequently and justifies this sort of specific treatment. "The specificity of this section has no doubt prevented much litigation." Exhibit p. 5.

Mr. Deeringer suggests that the concern about ascertaining the transferor's intent could be addressed by expanding the provision:

21135. (a) Property given by a transferor during his or her lifetime to a beneficiary is treated as a satisfaction of ~~a testamentary gift~~ an at-death transfer to that person in whole or in part only if one of the following conditions is satisfied:

(1) The instrument provides for deduction of the lifetime gift from the ~~testamentary gift~~ at-death transfer.

(2) The transferor declares in a contemporaneous writing that the transfer is to be deducted from the ~~testamentary gift~~ at-death

transfer or is in satisfaction of the ~~testamentary gift~~ at-death transfer.

(3) The transferee acknowledges in writing that the gift is in satisfaction of the ~~testamentary gift~~ at-death transfer.

(4) A court finds that the lifetime transfer was intended by the transferor to be in satisfaction of the at-death transfer.

(b) Subject to subdivision (c), for the purpose of partial satisfaction, property given during lifetime is valued as of the time the transferee came into possession or enjoyment of the property or as of the time of death of the transferor, whichever occurs first.

(c) If the value of the gift is expressed in the contemporaneous writing of the transferor, or in an acknowledgment of the transferee made contemporaneously with the gift, that value is conclusive in the division and distribution of the estate.

Respectfully submitted,

Nathaniel Sterling
Executive Secretary

ESTATE PLANNING, TRUST
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July 11, 2000

California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

Re: **Rules of Construction: Probate Code Sections 21101-21140**

Dear Commissioners and Staff:

On behalf of the Executive Committee of the Estate Planning, Trust, and Probate Law Section of the State Bar, I have reviewed Professor McGovern's March 2000 study on the Probate Code rules of construction. Unfortunately, I am not able to attend the Commission's July 20, 2000 meeting and therefore must offer my comments in writing.

The following comments are all my own, except for the comments on Section 21110 (anti-lapse), which reflect input from the Executive Committee as a whole.

§ 21102. Intention of transferor

The title of our existing §21102 is "Intention of Transferor" rather than "Intention of Testator", and I assume that Prof. McGovern's use of the word "testator" in his study was inadvertant and does not indicate an intention to change the title.

I agree that one should be able to consider extrinsic evidence of intent and not simply the intent "as expressed in the instrument". I also agree with Prof. McGovern's statement that the *rules of construction* should be subject to override by extrinsic evidence even if *express statements* in the instrument are not. However, Prof. McGovern's proposed revisions of this section appear to go beyond the implementation of these principles and give *too little* deference to the transferor's express statements of intent.

The wording of Prof. McGovern's proposed subsection (b) would require the parties to fall back on the rules of construction, even in the face of express statements of contrary intent in the instrument, unless a court (presumably) had found that such written expressions of intent did in fact reflect the transferor's intent. This would not be a helpful change in the law.

I suggest that subsection (b) read: **"The rules of construction expressed in this part apply in the absence of an express statement of intent in the instrument or a court finding of contrary intent on the part of the transferor."** This wording would allow extrinsic evidence

to override the rules of construction but not express statements of intent, which is, I believe, the result we want.

§21104. "Testamentary gift" defined

The word "testamentary", as Prof. McGovern notes, is historically associated with wills; therefore, it is not obvious, as it should be, that the term "testamentary gift" is intended to apply to nonprobate as well as probate transfers. This problem becomes more significant than it would be otherwise if the term is inserted into revised §§21109 and 21110, as Prof. McGovern has suggested.

One could use the term "at-death transfer" instead, but that term may imply that only present interest transfers are included and not future interests (although the definition itself clears that up). As an alternative, one could retain the term "testamentary gift" but say that it means "a transfer in possession or enjoyment, *including a nonprobate transfer*, that takes effect at or after death." The term "at-death transfer" is frequently used by attorneys and other estate planning professionals in the tax planning context and is more obvious. I prefer that term to "testamentary gift", regardless how the latter is defined.

§§21109 and 21110: Survivorship and Anti-lapse

Effect of Survivorship Language. Prof. McGovern appropriately gives much attention in his discussion of these sections to the proper effect of words of survivorship in a transfer. I prepared a memorandum for my Executive Committee outlining this issue, the UPC approach, and the past and present California rules, and presenting Prof. McGovern's recommendations.

The Executive Committee overwhelmingly favors retaining California's current approach to survivorship language, namely, that an express requirement of survivorship indicates an intention that the anti-lapse rule *not* apply, at least to the extent that the instrument in question is lawyer-prepared.

We are not at all persuaded by the UPC Comment to the effect that words of survivorship tend to reflect the drafter's form language more than they do the transferor's intent. Our experience as drafting attorneys is to the contrary. First, a competent attorney *does* typically ask the client who states desire to make a transfer "to my children", for example, whether the client wishes to have the share of a predeceased child pass to his or her issue. Second, we use words of survivorship when the client has expressed to us an intention to benefit only the person or class members in question and not their issue. While the client may not fully understand how or why survivorship language accomplishes the goal of benefitting only the transferee or the surviving members of a

stated class, the drafting lawyer knows what such language accomplishes and (if the drafter is competent), he or she uses such language intentionally, to achieve the client's stated goal.

If the client wants the gift to pass to the issue of a predeceased transferee, the instrument will, in the case of a transfer to one individual, either omit any reference to survival or follow the survivorship language with an alternative gift to issue. If the client wants to benefit only the surviving members of a class, the instrument will either (a) divide the property in question into shares, with the share of a predeceased class member passing to his or her issue, or (b) include words of survivorship but follow those words with an alternative gift to issue. Words of survivorship, *without more*, do not, in our experience, imply an intent to benefit the issue of a predeceased transferee.

Each of us on the Executive Committee who is in private practice has drafted many hundreds of transfers of tangible personal property, in particular, which include words of survivorship without a following alternative gift to issue. We know that our clients in these cases did not wish to have the share of any predeceased child pass to his or her issue. A change in the anti-lapse rule, applied to all instruments regardless of the time of execution, would create a great many administration problems and require the sale of tangible personal property in many cases where no such sale was contemplated by the transferor.

Prof. McGovern's recommendation apparently would allow for override of the anti-lapse rule in the case of a transfer "to my sister, Dolly Donee, if she survives me," but it would cause the rule to apply in the case of a class gift that uses survivorship language. We cannot see any reason to make a distinction in this respect between gifts to one individual and class gifts.

However, our Executive Committee discussion did not reach the question whether the anti-lapse statute should trump survivorship language in the case of *beneficiary designations* (as opposed to wills, trusts, and other attorney-drafted instruments). In such cases one cannot suppose that the attorney's form book has determined the expression of the gift; instead, the transferor has more likely used his or her own words. Is a layperson likely to use words of survivorship when he or she really intends to benefit the issue of a predeceased designee? I believe it is more likely that a layperson's use of survivorship language reflects an intention to benefit the named person only or the surviving members of the described class.

In any event, a distinction between attorney-drafted transfers and non-attorney drafted transfers would be difficult to draft into the statute. I suspect that if the question were posed to them, the Executive Committee would prefer a uniform rule that gives effect to survivorship language.

Vesting of Future Interests. I concur with Prof. McGovern's recommendation concerning the vesting of future interests. The Executive Committee's initial reaction to the issue was the

same as mine, although most conceded that the issue was a little too involved for them to give a final and definitive opinion after five minutes of discussion, my earlier memo notwithstanding. We may ultimately get some dissent on this question, but I doubt that the committee as a whole will adopt a contrary view.

A couple of additional comments on Prof. McGovern's proposed language:
(1) For reasons explained above in my discussion of §21104, we may create less confusion by using the term "at-death transfer" instead of "testamentary gift".
(2) Do we need to refer to an "instrument *of transfer*"? The term "instrument" is defined adequately in §45 and is used elsewhere in the Rules of Construction without modifiers. I suggest that we simply refer to an "instrument".

§21116. Testamentary disposition vests at death

I agree with Prof. McGovern's observation that this section is in conflict with the rule that postpones vesting of future interests until the time when the interest vests in current enjoyment. At a minimum, this section must be made inapplicable to future interests.

However, this section may still be useful as it applies to dispositions of present interests. In the administration of decedent's estates and trusts, it is helpful to have authority for the proposition that a beneficiary of a present interest is the *owner* of that interest as of the moment of death, subject only to administration of the estate or trust.

If the section is retained in any form, we will have to deal with the appropriateness of the term "testamentary disposition". As Prof. McGovern notes elsewhere in his study, the term contrasts with the term "testamentary gift", which is defined in §21104. In my discussion of §21104 above, I suggested the term "at-death transfer" as a substitute for "testamentary gift".

If my suggested terminology were used, the section could perhaps read: **"An at-death transfer of a present interest is presumed to vest at the transferor's death."** When I rephrase the statute in this manner, it seems so self-evident that I am more inclined to agree with Prof. McGovern after all. Maybe we don't need this section at all.

§21120. Avoidance of intestacy

I disagree with the statement that courts pay only lip service to the concept of avoiding intestacy, and I believe it would be helpful to draft this section in a manner that applies the principle to transfers by trust as well as by will.

Perhaps the last sentence of the section could read: **"Preference is to be given to an interpretation of an instrument that will prevent failure of a transfer rather than to one that will result in a failed transfer."**

§§21133 and 21134. Rights of recipient of specific gift

These two sections deal with various situations where ademption can fairly be presumed *not* to have been the transferor's intention. Prof. McGovern questions whether California courts really need statutory guidance in such cases.

I agree that our courts would probably decide cases presenting the statutory facts in the same manner as the statute provides. However, do we want to require the courts to make these decisions? The virtue of specific statutes such as §§21133 and 21134 is that they foreclose litigation (and even the necessity of uncontested petitions for orders determining entitlement to distribution) by leaving no doubt as to the proper result in such cases. Unless California courts have unambiguously and uniformly ruled on each of the questions presented in these sections, I would not favor simply repealing the section.

§21135. Satisfaction of testamentary gift

I would not want to see this section repealed. The premature satisfaction problem arises frequently and, in my view, justifies this sort of specific treatment. The specificity of this section has no doubt prevented much litigation.

I agree that the section leaves no room for introduction of *other* evidence of the transferor's intent. Perhaps a subdivision (3) should be added to subsection (a), reading as follows: **"(3) A court finds that the lifetime transfer was intended by the transferor to be in satisfaction of the at-death transfer."**

Again, the term "testamentary gift" should be reconsidered and the term "at-death transfer" perhaps substituted.

Incidentally, §21135, as quoted in the study, omits subsection (c).

By copy of this letter, I am informing my fellow members of the Estate Planning Committee of the Executive Committee of my comments and inviting them to concur or disagree. As I receive further comments from other committee members, I will pass them along to you.

We want to express our appreciation to Prof. McGovern for his thorough and well-considered study and to the Commission for undertaking a re-examination of the rules of construction.

Very truly yours,

James L. Deeringer

JLD:me

cc: James B. Ellis
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