

First Supplement to Memorandum 88-19

Subject: Study L-1030 - Fees of Corporate Trustees (State Bar Letter)

Attached to this supplement is a letter from Ken Klug on behalf of the Executive Committee of the State Bar Estate Planning, Trust and Probate Law Section concerning corporate trustees' fees. Attached to Mr. Klug's letter is a draft statute prepared by three members of the Executive Committee for consideration by the Commission if it is decided that a legislative solution is desirable.

The staff has not analyzed this draft since it is premature to do so until the Commission has considered Memorandum 88-19 and Assemblyman Harris' letter and decided if any additional information is needed. After that decision has been made, the staff will consider Mr. Klug's draft along with other possible remedies.

Respectfully submitted,

Stan G. Ulrich
Staff Counsel

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February 8, 1988

Mr. John H. DeMouilly
Executive Secretary
California Law Revision Commission
Suite D-2
4000 Middlefield Road
Palo Alto, California 94303-4739

Re: Memo 88-19

Dear John:

The Executive Committee of the Estate Planning, Trust and Probate Law Section has considered the issue of whether or not the size of corporate trustees' fees poses a problem to trust beneficiaries. It is the consensus of the members of the Executive Committee that any abuse which may exist is not of sufficient gravity to warrant corrective legislation. Generally, it has been our experience that where beneficiaries have a reasonable complaint about the size of the corporate trustees' fees, corporate trustees have willingly stepped aside in favor of either another corporate trustee whose fee schedule is lower, or in favor of an individual trustee. That informal practice has eliminated a great many of the fee problems.

Nonetheless, our Executive Committee recognizes that our experience may not be the universal experience. Indeed, Assemblyman Harris indicates in his February 1, 1988, letter to you that "arguably a greater number [of trust beneficiaries] who do not contact counsel have been adversely affected by increases in fees. . . ." In the event that the Commission perceives a problem needing a legislative solution, our Executive Committee is willing to work with you to draft a solution.

Mr. John H. DeMouilly
February 8, 1988
Page 2

I am enclosing for your review a rough draft of tentative legislation which takes one approach towards a legislative solution. This legislation could be added as Article 6 of Chapter 1 of Part 3 of Division 9 of the Probate Code. This approach would formalize the established informal practice, and provide an economical method of replacing an existing trustee in the event the existing trustee's fees exceed a certain threshold. (For our draft purposes, the threshold is tentatively set at 1 percent of the fair market value of the trust.) The enclosed draft goes somewhat further than merely addressing the problem raised by Assemblyman Harris: it provides an inexpensive means of appointing a successor trustee in those cases where the existing trustee agrees to resign. The enclosed draft is the product of three members of the Executive Committee, and has not yet been reviewed or approved by the entire Executive Committee. Accordingly, it does not represent the views of the Executive Committee.

Furthermore, this draft is not yet intended to be offered as legislation in its present form. There are still a number of practical problems with this approach which will need to be resolved by further refinements. Before working further to refine this draft, we would like the Commission's views as to whether the approach taken by this draft provides an appropriate solution. If so, we will be happy to undertake the work necessary to further refine this draft into workable legislation. If the Commission endorses this approach, we could have our final product to you by the end of April.

Very truly yours,



Kenneth M. Klug

Enclosure

cc: The Honorable Elihu M. Harris
L. Bruce Norman
David W. Lauer
John L. McDonnell, Jr.

To be Added to Probate Code, Division 9, Part 3, Chapter 1

ARTICLE 6

Replacement of Trustees

§15690. Right to Replace Trustee. If the reasonable compensation to which the trustee is entitled pursuant to §15681 during any 12-month period exceeds one percent (1%) of the average fair market value of the trust estate during such 12-month period, the trustee may be replaced as provided in this Article.

§15691. Notice of Excess Compensation. If the compensation received or to be charged by the trustee during any 12-month period exceeds 1% of the average fair market value of the trust estate during such period, then the trustee shall notify all beneficiaries of their right to replace the trustee as provided in this Article. The notice required by this Section shall be given not later than the earlier of (a) 30 days after the receipt by the trustee of such excess compensation or (b) 30 days after the trustee knows its compensation will exceed such 1%.

§15692. Form of Notice. [To be drafted.]

§15693. Procedure for Replacement. (a) If the trustee and all beneficiaries consent to replacement of the trustee, the

Draft, 12/11/87

trustee to be replaced may resign as provided in Article 3 and deliver the assets to the successor trustee, if any, named in the trust instrument. If there is no successor trustee named in the instrument, a successor trustee shall be selected as provided in §15694. A trustee who resigns pursuant to this subsection (a) shall be entitled to a reasonable termination fee.

(b) If all beneficiaries consent to a replacement trustee pursuant to this Article, and the trustee refuses to resign, the beneficiaries may petition the court for replacement of trustee as provided in §15695. If the court determines that the trustee unreasonably refused to resign, it shall award attorneys' fees and costs against the trustee.

(c) If some but not all beneficiaries consent to a replacement trustee, any person interested in the estate may petition the court for replacement of trustee as provided in §15695.

§15694. Selection of Replacement Trustee. A replacement trustee shall be selected as follows:

(a) If the trust instrument names a successor trustee who consents to act, the successor trustee shall be the replacement trustee.

(b) If the trust instrument does not name a successor trustee but provides a practical method of appointing a trustee, the replacement trustee shall be appointed as

Draft, 12/11/87

provided in the trust instrument.

(c) If neither subsection (a) nor subsection (b) is applicable, a replacement trustee shall be selected by the unanimous consent of all beneficiaries.

(d) If unanimous consent of all beneficiaries cannot be obtained, a replacement trustee may be appointed by the court on petition by any person interested in the trust.

(e) If the replacement trustee is not a corporate trustee, the court may require bond unless waived by the trust instrument or unless all beneficiaries consent to waiver of bond.

§15695. Court Findings. Upon petition by any beneficiary, the court shall replace a trustee if it finds all of the following:

(a) The compensation received or to be charged by the trustee for any 12-month period exceeds 1% of the average fair market value of the trust estate during such period.

(b) There is a replacement trustee qualified to administer the trust who has consented in writing to appointment as trustee.

(c) The compensation to be paid to the replacement trustee plus the premium to be charged to the trust estate for any bond required by the court are reasonably expected to be sufficiently lower than the compensation paid or to be paid the existing trustee to justify replacement.

Draft, 12/11/87

(d) Replacement of the existing trustee is to the best interest of all beneficiaries.

§15696. Definitions.

(a) "Average fair market value" means the greater of (i) the median of the fair market value on the first day of any 12-month period and the fair market value on the last day of the 12-month period; or (ii) the mean of the fair market values determined on a regular cycle.

(b) "All beneficiaries" means the person, if any, holding the power to revoke the trust; or, if none, the holder of a presently exercisable general power of appointment or power to withdraw property from the trust, to the extent of the holder's power over the trust property; or, if none, all adult beneficiaries who are receiving or are presently entitled to receive income under the trust or to receive a distribution of principal if the trust were terminated at the time consent is sought.