

Memorandum 91-38

Subject: Study L-3002 - Powers of Appointment (Exercise of Power by Residuary Clause in Will)

At the April meeting, the Commission approved the proposal to move the power of appointment statute from the Civil Code to the Probate Code. The proposal was approved by the representatives of the Executive Committee of the State Bar Estate Planning, Trust and Probate Law Section, the Probate and Trust Law Section of the Los Angeles County Bar Association, and the Legislative Committee of the Probate, Trust and Estate Planning Section of the Beverly Hills Bar Association present at the meeting. The Commission also approved the suggestion to include this proposal in the general probate bill in this legislative session, if we have the opportunity to make additional amendments to the bill (SB 271).

The only remaining issue concerns whether the section concerning exercise of a power of appointment by a residuary clause in a will should be revised in incorporate the new rule of the Uniform Probate Code. This issue arises because the pre-existing rule was adopted in 1981 based on the earlier UPC rule. Since the bar representatives had not had a chance to review this issue, it is presented again in this memorandum.

As adopted in 1981, Civil Code Section 1386.2 reads:

1386.2. A general residuary clause in a will, or a will making general disposition of all the testator's property, does not exercise a power of appointment held by the testator unless specific reference is made to the power or there is some other indication of intention to exercise the power. [Emphasis added.]

This section adopted the substance of Uniform Probate Code Section 2-610 (1979).

This 1981 revision reversed the rule of the former California section which provided that a general power of appointment was

exercised by a residuary clause or other general language of the donee's will purporting to dispose of property of the kind covered by the power unless the creating instrument otherwise required or the donee manifested an intent not to exercise the power.

In 1990, the UPC was revised to adopt a more sophisticated approach. The new rule, now located in UPC Section 2-608, provides as follows:

2-608. Exercise of power of appointment.

In the absence of a requirement that a power of appointment be exercised by a reference, or by an express or specific reference, to the power, a general residuary clause in a will, or a will making general disposition of all of the testator's property, expresses an intention to exercise a power of appointment held by the testator only if (i) the power is a general power and the creating instrument does not contain a gift if the power is not exercised or (ii) the testator's will manifests an intention to include the property subject to the power.

The revised UPC section is explained in greater detail in the UPC comment, which is attached as Exhibit 1.

The effect of the new language is to distinguish between wills with a gift in default provision from less well-planned estates. The rule of existing Civil Code Section 1386.2 (the former UPC rule) -- that the power is not exercised by a general residuary clause without specific intent -- would still apply where there is a gift in default. But if there is no gift over, it is better for the appointive property to pass in the donee's estate than in the donor's. Note also that the introductory clause recognizes that the power of appointment may require a reference for its exercise.

The staff recommends adoption of the 1990 UPC rule set out in Section 2-608.

Respectfully submitted,

Stan Ulrich
Staff Counsel

Section 2-608. Exercise of Power of Appointment.

In the absence of a requirement that a power of appointment be exercised by a reference, or by an express or specific reference, to the power, a general residuary clause in a will, or a will making general disposition of all of the testator's property, expresses an intention to exercise a power of appointment held by the testator only if (i) the power is a general power and the creating instrument does not contain a gift if the power is not exercised or (ii) the testator's will manifests an intention to include the property subject to the power.

COMMENT

General Residuary Clause. As revised, this section provides that a general residuary clause (such as "All the rest, residue, and remainder of my estate, I devise to . . .") in the testator's will or a will making general disposition of all of the testator's property (such as "All of my

estate, I devise to . . .") expresses an intent to exercise a power of appointment held by the donee of the power only if one or the other of two circumstances or sets of circumstances are satisfied. One such circumstance (whether the power is general or nongeneral) is if the tes-

129

tator's will manifests an intention to include the property subject to the power. A simple example of a residuary clause that manifests such an intention is a so-called "blending" or "blanket-exercise" clause, such as "All the rest, residue, and remainder of my estate, including any property over which I have a power of appointment, I devise to . . ."

The other circumstance that expresses an intent to exercise a power by a general residuary clause or a will making general disposition of all of the testator's property is that the power is a *general* power and the instrument that created the power does not contain a gift over in the event the power is not exercised (a "gift in default"). In well planned estates, a general power of appointment will be accompanied by a gift in default. The gift-in-default clause is ordinarily expected to take effect; it is not merely an afterthought just in case the power is not exercised. The power is not expected to be exercised, and in fact is often conferred mainly to gain a tax benefit—the federal estate-tax marital deduction under section 2056(b)(5) of the Internal Revenue

Code or, now, inclusion of the property in the gross estate of a younger-generation beneficiary under Section 2041 of the Internal Revenue Code, in order to avoid the possibly higher rates imposed by the new federal generation-skipping tax. See Blattmachr & Pennell, "Adventures in Generation Skipping, Or How We Learned to Love the Delaware Tax Trap," 24 Real Prop.Prob. & Tr.J. 75 (1989). A general power should not be exercised in such a case without a clear expression of an intent to appoint.

In poorly planned estates, on the other hand, there may be no gift-in-default clause. In the absence of a gift-in-default clause, it seems better to let the property pass under the donee's will than force it to return to the donor's estate, for the reason that the donor died before the donee died and it seems better to avoid forcing a reopening of the donor's estate.

Cross Reference. See also Section 2-704 for a provision governing the meaning of a requirement that a power of appointment be exercised by a reference (or by an express or specific reference) to the power.

Section 2-608. Exercise of Power of Appointment.

In the absence of a requirement that a power of appointment be exercised by a reference, or by an express or specific reference, to the power, a general residuary clause in a will, or a will making general disposition of all of the testator's property, expresses an intention to exercise a power of appointment held by the testator only if (i) the power is a general power and the creating instrument does not contain a gift if the power is not exercised or (ii) the testator's will manifests an intention to include the property subject to the power.

COMMENT

General Residuary Clause. As revised, this section provides that a general residuary clause (such as "All the rest, residue, and remainder of my estate, I devise to . . .") in the testator's will or a will making general disposition of all of the testator's property (such as "All of my

estate, I devise to . . .") expresses an intent to exercise a power of appointment held by the donee of the power only if one or the other of two circumstances or sets of circumstances are satisfied. One such circumstance (whether the power is general or nongeneral) is if the tes-

129

tator's will manifests an intention to include the property subject to the power. A simple example of a residuary clause that manifests such an intention is a so-called "blending" or "blanket-exercise" clause, such as "All the rest, residue, and remainder of my estate, including any property over which I have a power of appointment, I devise to . . ."

The other circumstance that expresses an intent to exercise a power by a general residuary clause or a will making general disposition of all of the testator's property is that the power is a *general power* and the instrument that created the power does not contain a gift over in the event the power is not exercised (a "gift in default"). In well planned estates, a general power of appointment will be accompanied by a gift in default. The gift-in-default clause is ordinarily expected to take effect; it is not merely an afterthought just in case the power is not exercised. The power is not expected to be exercised, and in fact is often conferred mainly to gain a tax benefit—the federal estate-tax marital deduction under section 2056(b)(5) of the Internal Revenue

Code or, now, inclusion of the property in the gross estate of a younger-generation beneficiary under Section 2041 of the Internal Revenue Code, in order to avoid the possibly higher rates imposed by the new federal generation-skipping tax. See Blattmachr & Pennell, "Adventures in Generation Skipping, Or How We Learned to Love the 'Delaware Tax Trap,'" 24 Real Prop.Prob. & Tr.J. 75 (1989). A general power should not be exercised in such a case without a clear expression of an intent to appoint.

In poorly planned estates, on the other hand, there may be no gift-in-default clause. In the absence of a gift-in-default clause, it seems better to let the property pass under the donee's will than force it to return to the donor's estate, for the reason that the donor died before the donee died and it seems better to avoid forcing a reopening of the donor's estate.

Cross Reference. See also Section 2-704 for a provision governing the meaning of a requirement that a power of appointment be exercised by a reference (or by an express or specific reference) to the power.