#L-3013

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09/12/90

First Supplement to Memorandum 90-126

Subject: Study L-3013 - Uniform Statutory Rule Against Perpetuities (Letter from Professor Dukeminier)

Attached is a letter from Professor Jesse Dukeminier concerning the double-pronged perpetuities saving clause language discussed in Memorandum 90-126, at pages 6-7.

Respectfully submitted,

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September 12, 1990

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
4000 Middlefield Road, Suite D-2
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FAX # 415-494-1827

Dear John:

RE: USRAP

I have the staff report dated 9/4/90 recommending adopting the amendment to the Uniform Statutory Rule Against Perpetuities adopted in July by the National Conference of Commissioners on Uniform State Laws. You really ought to take a careful look at this amendment. It creates an entirely new perpetuities trap for the unwary.

In essence, this amendment provides:

> If a trust termination clause calls for termination of the trust upon (1) the expiration of a period of years in excess of 21 <u>or</u> (2) the expiration of specified lives in being (plus 21 years, if the drafter so chooses), <u>whichever is later</u>, the first termination date will be disregarded and the trust will terminate upon the latter event.

The amendment prohibits giving effect to a double-prong termination clause of the type described. As a matter of perpetuities policy, such prohibition makes little sense. If a settlor can create a trust for either 90 years or lives in being plus 21 years, as USRAP provides, why should the settlor be prohibited from creating a trust for whichever period turns out to be longer?

More important, this prohibition of a double-prong clause creates a trap for persons who are acting quite reasonably and are not reaching for the maximum perpetuities period or for tax advantages. The operation of this amendment can be illustrated by the well-known case of Chun Quan Yee Hop, 52 Hawaii 40, 469 P.2d 183 (1970). In this case the testator created a trust for his issue for 30 years or until the death of his wife, whichever should occur last. Under the USRAP amendment, the trust is good only for the wife's life, and if the wife dies three years later, the testator's intent is almost completely defeated. Yet the testator could have had a 90-year trust had he wanted! Surely people who understand that a 90-year trust is valid will be

surprised to find out that a trust for 30 years or the life of the testator's widow will not be given effect.

Other examples of the trap created by this amendment: A trust for charity for 40 years or the lives of the settlor's adult children, whichever proves longer, will stop paying income to charity when the children die, maybe in a few years, defeating the settlor's intent. A trust for the settlor's issue for 25 years, with the settlor retaining the right to lifetime income, will apparently terminate upon the settlor's death, not upon the later expiration of 25 years.

The USRAP amendment was apparently adopted in an attempt to secure Treasury's blessing of a generation-skipping tax exemption for a 90-year trust. Treasury has been concerned that aggressive lawyers for the very rich in USRAP states will seek the maximum tax exemption period of 90 years <u>or</u> lives in being plus 21 years, whichever proves longer, creating an unfair tax disadvantage for non-USRAP states governed by the lives-in-being-plus-21-year period. Hence, under the expected Treasury ruling, the GST tax exemption will be allowed for 90 years or for lives in being plus 21 years, but not for whichever period proves longer.

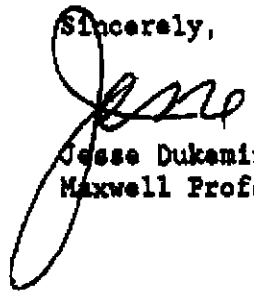
USRAP now offers you a choice of traps:

(1) Adopt the amendment and create a trap for a person who is not interested in GST tax exemption and is not seeking the maximum perpetuities period (as in the Chun case); or

(2) Reject the amendment and create a trap for a person who is seeking a GST tax exemption for the maximum perpetuities period and is unknowledgeable about Treasury regulations.

It seems to me that the amendment is an abdication of the policy said to underlie USRAP: protecting persons who consult lawyers unskilled in perpetuities law who do perfectly reasonable things (as in Chun). Where a choice of evils must be made, I believe the onus should be put upon those better able to avoid the evil -- in this case, on skilled estate planners who are more likely to know the tax rules and draft with them in mind. I do not think persons of moderate wealth who consult average lawyers should have their trusts struck down so that skilled lawyers for millionaires, in aggressively seeking GST tax advantages, will not inadvertently run afoul of a Treasury rule.

Sincerely,



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