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Re: unconstitutionality of amendments to ARS sec. 14-2901

Senator Bedford, Representatives Gonzales and Saldate,

I am a resident of your district, writing to ask whether one or another of you might ask the attorney general for a formal opinion. As you know, the AG does not issue opinions to private citizens.

The question is whether either or both of two separate amendments to ARS sec. 14-2901 violates section 9 of Article II of the state constitution. That section says "no law shall be enacted permitting any perpetuity or entailment in this state."

The framers intended this prohibition as a safeguard against the unreasonable accumulation of wealth in the hands of a few families, which they viewed as a threat to the viability of a representative democracy. The primary form of wealth has since migrated from land to financial instruments, but the policy concern is if anything more urgently compelling today.

For many years, ARS sec. 33-261 and its predecessors gave statutory substance to the constitutional language by incorporating the common law rule against perpetuities. The common law rule says a nonvested interest in property is not valid unless it is certain to vest or fail within twenty-one years after the death of some person who is alive at the time the interest is created -- or to put it another way, any contingencies on which a future interest depends must by their own terms be certain to resolve within that time.

Under the common law rule, the validity or invalidity of a future interest is determined at the moment it is created. If there is a scenario under which vesting of an interest might be delayed beyond the period of the rule, that interest is invalid on day one.

The simplest example is a trust that is supposed to continue through multiple generations, benefiting great-great-grandchildren whose parents have not yet been born. But the rule can sometimes invalidate a future interest based on some scenario that seems extremely unlikely to occur. And for this reason, the rule has been criticized as highly technical, invalidating some transfers that do not actually offend the underlying policy.

It is in fact not difficult for a competent lawyer to draft around the rule, and courts have long been willing to reform a will or a trust to bring it into compliance with the rule. Nonetheless, in recent decades some state courts and quite a number of state legislatures have adopted a "wait and see" approach, validating any future interest that does in fact vest within the period of the rule. Allowing the unlikely scenarios to play out, in other words.

Arizona is among these. In 1994, the Arizona legislature enacted a ninety-year "wait and see" statute, largely tracking the provisions of a model developed by the National Conference of Commissioners on Uniform State Laws in the mid-1980s. This was codified at ARS sec. 14-2901 through 14-2906. ARS sec. 33-261 remains on the books, but it has been superseded by these sections.

My questions concern two subsequent amendments to ARS sec. 14-2901.

In 1998, the legislature added a paragraph 3 to subsection A of this section, abrogating the common law rule altogether if the future interest in question is in a trust and the trustee has a power of sale -- provided that someone who was alive when the trust was created has a power, exerciseable at some point after the trust was created, to terminate the interest.

It is not entirely clear what this latter proviso was intended to accomplish. Suffice it to say that if for example -- as is quite common -- a beneficiary in the first or second generation were given a limited power to appoint the trust remainder at his or her death and did not exercise it -- which again is quite common --, this apparently would meet the statutory requirement.

In short, with the enactment of SB 1112 a trust in Arizona may continue indefinitely if the trustee has ordinary investment powers. Paragraph 3 permits an "entailment" of the equitable interests in the trust until the end of time, preserving only that portion of the rule against perpetuities that deals with restraints on alienation of the underlying legal interests.

It may be the that attorney general will say the constitutional prohibition has to do only with restraints on alienation, and not with the remote vesting of future interests, but this is not at all obvious, and the word "entailment" suggests the contrary.

A future interest in a trust is itself "property." A beneficiary of a spendthrift trust cannot "alienate" his or her interest in the trust, even if the trustee has the power to sell trust assets and reinvest the proceeds.

Then, in 2008, the legislature amended paragraph 2 of subsection A, increasing the "wait and see" period for determining the validity of a nonvested future interest to five hundred years. Five hundred.

Ninety years is at least arguably within the interval contemplated by the common law rule -- lives in being plus twenty-one years. Five hundred years eviscerates the rule. Paragraph 1 immediately preceding, which paraphrases the common law rule, is rendered entirely meaningless. There is no circumstance under which a future interest would meet the requirements of the common law rule while failing the five hundred year "wait and see."

This amendment to ARS sec. 14-2901 was folded into a much larger bill, HB 2806, enacting rather comprehensive changes to the trust code, loosely modeled on another uniform act. The five hundred year "wait and see" period, which effectively abrogates the rule against perpetuities altogether, received less than scant attention in committee hearings.

The bill was drafted by a committee of the organized bar and supported by the state bankers association. Both these groups have a strong self interest in drawing fees from creating and maintaining these arrangements. Ordinary people without an axe to grind were given no practical opportunity to weigh in.

No one at any of the committee hearings asked about the constitutional issue, nor did anyone ask what might be the social consequences of abrogating the rule, though these are reasonably predictable:

> multiple generations of beneficiaries insulated from civil liability for their actions because their assets are tied up in perpetual spendthrift trusts;
>
> large pools of financial assets controlled by a handful of families -- or worse, a handful of corporate trustees --, who can then manipulate the mechanisms of government through their armies of bankers and lawyers;

and so on. Senator Bedford, who served in the House during the second regular session in 2008, can confirm these issues received exactly zero attention on the floor.

Again, it may be that the attorney general will say five hundred years is not forever. But it is a very, very long time. The history of the common law rule itself is usually traced to the Duke of Norfolk's Case, decided by the House of Lords in 1682, somewhat less than five hundred years ago.

Ultimately, I would also like to ask each of you to sponsor a bill to restore the statutory "wait and see" period to ninety years and to limit trust accumulations to the common law period. Of course, an opinion from the attorney general acknowledging either or both of the amendments to ARS sec. 14-2901 violates the state constitution would be helpful in moving such a bill forward.

Sincerely,

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