

Memorandum 2001-37

Estate Planning and Dissolution of Marriage: AB 873 (Harman)

In September 1998, the Commission issued a recommendation relating to the *Effect of Dissolution of Marriage on Nonprobate Transfers*. In October 2000, the Commission issued a recommendation relating to *Estate Planning During Marital Dissolution*. Both of these recommendations would be implemented by AB 873 (Harman).

The staff has provisionally agreed to some minor changes to the language in the Commission's recommendations. These changes are presented below for the Commission's consideration and possible ratification.

EFFECT OF DISSOLUTION OF MARRIAGE ON NONPROBATE TRANSFERS

In general terms, the recommendation relating to the *Effect of Dissolution of Marriage on Nonprobate Transfers* proposes that a nonprobate transfer to a spouse should fail by operation of law if the transferor and spouse are no longer married at the time of the transferor's death. Similarly, joint tenancy between former spouses would be severed (extinguishing the right of survivorship) if they are not married to each other at the time of one of their deaths. This would implement the intention of a typical divorcing person and would be consistent with existing law providing that dissolution or annulment of marriage automatically revokes a will provision benefiting a former spouse. Due to unfavorable political circumstances at the time the recommendation was issued, the Commission decided not to immediately seek introduction of legislation implementing it. The State Bar has now sponsored AB 873, which implements the recommendation.

AB 873 has been referred to the Assembly Judiciary committee. Donna Hershkowitz, counsel for the committee, raises two concerns regarding the bill: (1) The statutory warning language in Family Code Section 2024 should be clearer. (2) Language should be added to make clear that the proposed law does not affect the court's power to order that a nonprobate transfer (such as life

insurance) be continued in effect for the benefit of a former spouse. These concerns are discussed below.

Statutory Warning

Family Code Section 2024 provides that the petition and judgment forms for dissolution or annulment of marriage include specified language warning of the effect of dissolution or annulment of marriage on various property matters. The proposed law would modify the form language to read as follows:

Dissolution or annulment of your marriage may automatically affect the rights of your former spouse regarding such things as your will, life insurance proceeds, trust benefits, retirement death benefits, power of attorney designation, pay on death bank accounts, transfer on death vehicle registration, and joint tenancy survivorship. You should review these matters, as well as any credit cards, other credit accounts, and credit reports to determine whether they should be changed or reaffirmed in view of the dissolution or annulment of your marriage, or your legal separation. However, some changes may require the agreement of your spouse or a court order (see Part 3 (commencing with Section 231) of Division 2 of the Family Code).

Ms. Hershkowitz believes that the warning would be more understandable, especially to pro per litigants, if revised as follows:

Dissolution or annulment of your marriage may automatically affect the rights of your former spouse regarding change your spouse's rights to such things as your will, life insurance proceeds, trust benefits, retirement death benefits, power of attorney designation, pay on death bank accounts, transfer on death vehicle registration, and survivorship rights to any property taken in joint tenancy survivorship. If you do not want the dissolution or annulment of your marriage to interfere with the named beneficiary on such things, you must make that intention clear. Your rights to such things as your spouse's will, life insurance proceeds, trust benefits, retirement death benefits, power of attorney designation, pay on death bank accounts, transfer on death vehicle registration, and survivorship rights to any property taken in joint tenancy may also be automatically changed upon dissolution or annulment of your marriage. You should review these matters, as well as any credit cards, other credit accounts, insurance policies, retirement benefit plans, and credit reports to determine whether they should be changed or reaffirmed whether you should take any other actions in view of the dissolution or annulment of your marriage, or your legal separation. However,

some changes may require the agreement of your spouse or a court order (see Part 3 (commencing with Section 231) of Division 2 of the Family Code).

The staff has no objection to these changes. To the extent that they make the effect of the proposed law clearer, they are an improvement.

Authority of Court to Order Continuation of Nonprobate Transfer

Ms. Hershkowitz is concerned that the proposed law might be misunderstood as somehow limiting the authority of a court to order that a nonprobate transfer be maintained for the benefit of a former spouse. Such orders are fairly common (especially with respect to life insurance).

The proposed law already provides that a nonprobate transfer does not fail if “The nonprobate transfer is not subject to revocation by the transferor at the time of the transferor’s death.” See proposed Prob. Code § 5600(b)(1). The Comment to proposed Section 5600(b)(1) elaborates:

This precludes operation of subdivision (a) where a nonprobate transfer is irrevocable on execution, or later becomes irrevocable by the transferor (for reasons other than the death or incapacity of the transferor). For example, a court may order a spousal support obligor to maintain life insurance on behalf of a former spouse. See Fam. Code § 4360. If a person dies while subject to such an order, subdivision (a) would not affect the rights of the transferor’s former spouse under the policy.

Ms. Hershkowitz agreed that this addresses her concern, but feels that reinforcing language should be added to the statute itself. She proposes adding an exception to proposed Section 5600(b) as follows:

5600. ...

(b) Subdivision (a) does not cause a nonprobate transfer to fail in either of the following cases:

(1) The nonprobate transfer is not subject to revocation by the transferor at the time of the transferor’s death.

(2) There is clear and convincing evidence that the transferor intended to preserve the nonprobate transfer to the former spouse.

(3) A court order that the nonprobate transfer be maintained on behalf of the former spouse is in effect at the time of the transferor’s death.

In addition, Ms. Hershkowitz proposes adding the following provision:

5604. Nothing in this part is intended to limit the court's authority to order a party to a dissolution or annulment of marriage to maintain the former spouse as a beneficiary on any nonprobate transfer described in this part, or to preserve a joint tenancy in favor of the former spouse.

While the staff thinks that the original language was adequate, these additions would not change the substance of the proposed law and would make it clearer that the proposed law does not override a court order to maintain a nonprobate transfer for the benefit of a former spouse.

If the Commission ratifies these changes, the Comments to these sections should be revised as follows:

Comment. Section 5600

Paragraph (1) of subdivision (b) provides that a nonprobate transfer to a former spouse does not fail by operation of subdivision (a) if, at the time of the transferor's death, the nonprobate transfer is not subject to revocation by the transferor. This precludes operation of subdivision (a) where a nonprobate transfer is irrevocable on execution, or later becomes irrevocable by the transferor (for reasons other than the death or incapacity of the transferor). Paragraph (3) makes clear that an effective court order requiring that a nonprobate transfer be maintained for the benefit of a former spouse prevents the failure of a nonprobate transfer pursuant to subdivision (a). For example, a court may order a spousal support obligor to maintain life insurance on behalf of a former spouse. See Fam. Code § 4360. If a person dies while subject to such an order, subdivision (a) would not affect the rights of the transferor's former spouse under the policy. The irrevocability of a trust can be established by certification of the trust's contents. See Section 18100.5.

Comment. Section 5604 is new.

ESTATE PLANNING DURING MARITAL DISSOLUTION

Under existing law, an automatic temporary restraining order (ATRO) restrains the disposition of property during a proceeding for dissolution or annulment of marriage, or legal separation. Fam. Code § 2040. The *Estate Planning During Marital Dissolution* recommendation would provide that the ATRO restrains estate planning changes that can affect a spouse's property interests (such as modification of the beneficiary of a trust), but does not restrain

estate planning changes that cannot affect a spouse's property interests (such as revocation of a revocable trust).

The State Bar indicated that it would sponsor legislation implementing this recommendation. However, miscommunication within the Bar delayed formal approval of the decision to sponsor the legislation. The staff then suggested to the Bar's lobbyist, Larry Doyle, that AB 873 could be amended to include the language proposed in the recommendation, based solely on the Commission's recommendation. The bar could be added as a sponsor later, once it had formally approved that action. Mr. Doyle was amenable to this idea and presented it to Assembly Member Harman's staff. It now appears that AB 873 will be amended to include the *Estate Planning During Marital Dissolution* material.

Both the State Bar and Donna Hershkowitz have proposed minor changes to the proposed law. These are discussed below:

State Bar Suggestions

The Executive Committee of the State Bar Estate Planning, Trust, and Probate Law Section ("ExComm"), has proposed a number of minor changes to proposed Family Code Section 2040(b):

- (b) Nothing in this section restrains any of the following:
 - (1) Creation, modification, or revocation of a will.
 - (2) Revocation of a nonprobate transfer, including a revocable trust, pursuant to the instrument.
 - (3) Elimination of a right of survivorship to property.
 - (4) Creation of an unfunded revocable or irrevocable trust.
 - (5) Execution and filing of a disclaimer pursuant to Part 8 (commencing with Section 260) of Division 2 of the Probate Code.

These appear to be nonsubstantive clarifying changes and the staff has no objection to the suggested language.

Suggestions of Ms. Herkowitz

The staff met with Ms. Hershkowitz and Mr. Doyle to discuss amendment of AB 873 to include the *Estate Planning During Marital Dissolution* material. Ms. Hershkowitz had one concern about the proposed law: if one party can unilaterally revoke a trust, that will free up the trust assets, increasing the likelihood that those assets might be dissipated or hidden. She proposes that a person who revokes a nonprobate transfer during a dissolution proceeding should be required to provide notice of the action to his or her spouse. The

spouse would then be in a better position to protect against dissipation or concealment of marital property. She indicated that the bill might not pass the committee if a notice requirement were not added.

The staff does not believe that allowing revocation of a nonprobate transfer would significantly increase the likelihood of dissipation or concealment of assets subject to the nonprobate transfer. The ATRO already restrains any transfer of property. In order to improperly dispose of assets subject to a revoked nonprobate transfer, a person would need to violate that general provision of the ATRO. A person willing to violate the ATRO in order to misappropriate marital assets would probably not comply with a notice requirement. However, the staff believes that a notice requirement is sensible for other reasons. If a person makes significant changes to an instrument governing disposition of marital property in the course of a dissolution proceeding, it seems reasonable that the person's spouse should be informed. The spouse would then be alerted that an element of the spouse's estate plan has been changed, and that the spouse may need to adjust his or her estate plan in light of the change. Notice may also alert a spouse of the need to make similar changes to other instruments. Considering the generally beneficial effect of a notice requirement, the staff recommends that a notice provision be added. This could be implemented by amending proposed Section 2040(b) as follows:

(b) Nothing in this section restrains any of the following:

(1) Creation, modification, or revocation of a will.

(2) Revocation of a nonprobate transfer, including a revocable trust, pursuant to the instrument, provided that notice of the change is filed and served on the other party before the change takes effect.

(3) Elimination of a right of survivorship to property, provided that notice of the change is filed and served on the other party before the change takes effect.

(4) Creation of an unfunded revocable or irrevocable trust.

(5) Execution and filing of a disclaimer pursuant to Part 8 (commencing with Section 260) of Division 2 of the Probate Code.

Comment. ...

Subdivision (b)(2) provides that the restraining order does not restrain revocation of a nonprobate transfer, provided that notice of the change has been filed and served on the other party. This does not mean that a nonprobate transfer is necessarily subject to revocation by one party without the consent of the other party. The question of whether a nonprobate transfer is subject to unilateral

revocation is governed by the terms of the nonprobate transfer and applicable substantive law. See, e.g., Prob. Code § 5506 (action by all surviving joint owners required to cancel beneficiary registration of jointly-owned security); 31 C.F.R. § 353.51 (2000) (restricting changes in ownership of jointly-owned Series EE savings bond).

Subdivision (b)(3) provides that the restraining order does not restrain elimination of a right of survivorship, provided that notice of the change has been filed and served on the other party. This codifies is consistent with *Estate of Mitchell*, 76 Cal. App. 4th 1378, 91 Cal. Rptr. 2d 192 (1999) (restraining order does not restrain severance of joint tenancy).

There are two noteworthy aspects of the language set out above: (1) It applies only to changes that can affect marital property — changes to a will, creation of an unfunded trust, and execution of a disclaimer are *not* affected. (2) Filing and service is required. This is intended to ensure that there is a record of the notice, in case the validity of the revocation or severance is subsequently challenged on the basis of an alleged failure to provide the required notice.

CONCLUSION

All of the changes discussed above are minor, and with the exception of the notice requirement, all are nonsubstantive. The staff recommends that the Commission approve these changes. If the Commission disagrees with any of these changes, the staff will need to work with the State Bar, Ms. Hershkowitz, and the author's office to seek an acceptable alternative.

Respectfully submitted,

Brian Hebert
Staff Counsel