

Memorandum 92-77

Subject: Study F-1010 - Family Code (Definition of Community Estate)

We have received a suggestion by James Endman, Los Angeles County Superior Court Commissioner, for reorganizing the definitions of "community estate" in the Family Code. (See Exhibit 1.) Others have expressed dissatisfaction with the fact that the Family Code contains two different definitions of "community estate" -- in Section 901 concerning liability of marital property for debts and in Section 2501 concerning division of property on dissolution of marriage or legal separation. For example, Frieda Gordon Daugherty, writing on behalf of the Association of Certified Family Law Practitioners, has asked why community estate includes quasi-community property sometimes but not others. (See Exhibit 2, attached to the First Supplement to Memorandum 92-32, considered at the May 1992 meeting.) Ms. Daugherty suggests that it would be preferable to have one definition.

Family Code Section 901, applicable to creditors' rights, provides as follows:

901. "Community estate" includes both the community property and the quasi-community property.

Existing Civil Code Section 5120.020, which is superseded by Family Code Section 901, defines "community property" to include quasi-community property. The staff is convinced that the approach of Family Code Section 901 is indisputably superior to Civil Code Section 5120.020. A term should not be defined to include another term that it normally does not include. The term "community estate" is handy, useful, and appropriate.

Family Code Section 2501, applicable to division of marital property, provides as follows:

2501. "Community estate" includes both the community property and the quasi-community assets and liabilities of the parties.

This definition is identical to the language of the last paragraph of Civil Code Section 4800(a).

The term "community estate" is also used in one section in an undefined sense. Family Code Section 1101(a) provides as follows:

1101. (a) A spouse has a claim against the other spouse for a breach of the fiduciary duty imposed by Section 1100 or 1102 that results in impairment to the claimant spouse's present undivided one-half interest in the community estate, including, but not limited to, a single transaction or a pattern or series of transactions, which transaction or transactions have caused or will cause a detrimental impact to the claimant spouse's undivided one-half interest in the community estate. [Emphasis added.]

This language is the same as existing Civil Code Section 5125.1(a), except for cross-reference adjustments and correction of a typographical error in the existing section. (Existing law refers to the "present undivided one-half interest in the community interest" -- this has been changed to community estate for consistency with the final clause of the sentence.) The Commission will recall that the sections concerning management and control of marital property and fiduciary duties between spouses were revised during the legislative process to satisfy objections made by the Los Angeles Women's Leadership Network. The Commission agreed to include the existing structure and language of Civil Code Sections 5103, 5125, 5125.1, and 5127, with a few technical changes that were mutually agreed upon.

There are two problems with simply adopting Commissioner Endman's proposal to make a single definition of "community estate" apply to the entire Family Code. First, the "assets and liabilities" feature must be preserved in the rules on division so that it is clear that community liabilities are subject to division as are community assets. This problem can be dealt with by some remedial drafting in the part of the code concerning division of marital property.

The second problem concerns applying a definition that includes quasi-community property to the fiduciary duty provision in Section 1101(a). This issue has not been addressed by any of the commentators who have been troubled by the definitions or suggested revisions. Application of the suggested community estate definition to Family Code Section 1101(a) could be seen as changing the substance of this statute

by roping quasi-community property into the inter-spousal fiduciary claims procedure. In addition to being an unintended or unwarranted substantive change, it may be unconstitutional.

The staff sees several ways to preserve the fiduciary duty statute without substantive change while attempting to satisfy the concern raised by Commissioner Endman and others:

(1) Make Language Internally Consistent

The sections in the Civil Code concerning management and control and fiduciary duties between spouses use the term "community estate" only once. (See Civ. Code §§ 5103, 5125, 5125.1, 5127; see also Fam. Code §§ 721, 1100-1102.) Usually references are made to community property, although some other variations are used, such as "assets in which the community has or may have an interest." (There is also a reference to "separate estate" in Section 5125, but this does cause any perceptible problems because the term is nowhere defined.) Section 5125.1 establishes a spouse's claim against the other spouse for breach of the fiduciary duty imposed by Section 5125 or 5127. Neither of these sections uses "community estate." Nor does Section 5103, incorporated by Section 5125, refer to the "community estate."

What then is meant by "community estate" in Civil Code Section 5125.1(a)? Perhaps sponsors of the 1986 legislation that enacted this section will be able to assist the Commission on the issue. The staff has found nothing in researching the matter to suggest that the reference was meant to include quasi-community property. The consultant's analysis of the 1986 bill, following the amendment that inserted "estate" in place of "property," does not refer to the term. (See Exhibit 2, Assembly Judiciary Committee Consultant's Analysis of SB 1071, as amended July 13, 1986, 1985-86 Regular Session; 1986 Cal. Stat. ch. 1091.)

The staff suspects that "community estate" in Civil Code Section 5125.1(a) is the same as "community property" as used in the rest of the section and in related sections, and that its purpose was to refer to the aggregate of community property, not just any particular item of property that may have been involved in a transaction giving cause to the claim for breach of fiduciary duty. Hence, Family Code Section 1101(a) could be amended to replace "community estate" with "the

aggregate of the community property" without changing the substance of the law. This would permit a general definition of "community estate" in Division 1 of the Family Code. This term could then be used consistently throughout the code, thereby avoiding the confusion that apparently results from the structure of existing law that was carried into the Family Code.

(2) Sidestep the Problem by Relying on Incorporation of Rights

Perhaps a better, more creative approach is to define community estate for the entire code to include both community and quasi-community property and make clear in relevant Comments, or elsewhere, that the definition is not intended to alter the rights of spouses as they apply under Family Code Section 1101. In other words, the effect of using "community estate" in Section 1101(a) would not change as a result of the new definition. This follows because Section 1101(a) applies to rights the spouse has ("undivided one-half interest in the community estate") as the result of the application of other law -- it does not create new property rights. So too, the new definition of community estate would not create new property rights.

(3) Create a New Term

The third approach would be to create a new term, such as "marital estate," and define it to include community and quasi-community property. This approach would entail replacing "community estate" with "marital estate" in 23 Family Code sections in Division 4 (liability of marital property) and Division 7 (division of property), as well as in Section 2337 (severance and grant of early trial on issue of dissolution of status of marriage). The virtue of this approach is that the usage of "community estate" in Section 1101 would remain untouched. It remains to be seen whether attorneys, judges, and other interested persons would find this a desirable development. We hope to hear their views.

(4) Drop the Term "Community Estate"

A fourth possibility would be to use the phrase "community and quasi-community property" every place where the defined term is used in the Family Code, i.e., everywhere but in Section 1101(a). The longer

phrase is obviously more cumbersome to read and can impede understanding in complicated sections. In addition, it would undo the amendments made to Civil Code Section 4800 in 1986 when "the community property and the quasi-community property" was replaced in a number of places by "the community estate" as defined in Section 4800(a). (See 1986 Cal. Stat. ch. 215, § 1.)

(5) Restrict "Community Estate" Definition to Property Division

The objection to having two definitions of the term could be met by returning to the situation existing in the Civil Code. This would mean defining community estate to include community and quasi-community property only for the property division provisions. This would leave Family Code Section 1101(a) untouched; "community estate" would mean whatever it means, without further definition. The property division definition in Family Code Section 2501 would continue the definition of existing Civil Code Section 4800(a). The definition in Section 901 would be eliminated and reference made to both community and quasi-community property, as in alternative (4). The staff does not think this is a particularly helpful solution, except that it does preserve existing law. It would not do anything to eliminate existing inconsistencies.

The staff recommends that the Commission pursue Court Commissioner Endman's suggestion concerning adopting one definition of community estate and applying it to the entire code. We trust that interested persons will be able to assist the Commission in determining the best way to achieve this goal, whether through one of the approaches suggested above or in some other manner.

Respectfully submitted,

Stan Ulrich
Assistant Executive Secretary

MEMO

DATE: September 30, 1992
TO: Frieda Daugherty
FROM: Commissioner Endman
SUBJECT: Family Code

Suggestion:

Change Section 65 to the definition included in Section 901, to wit:

Section 65. "Community estate" includes both the "community property" (as defined in Section 120) and the "quasi-community property" (as defined in Section 125).

add a new section 120:

Section 120: [include here the definition set forth in the present section 65]

Delete sections 901 and 2501 for the following reasons:
901 because it is now section 65 and 2501 because section 910 makes the community estate liable for debts.

Also: 2502 seems unnecessary after defining sections 125 and 130. It almost sounds juvenile to think that people could not know that quasi-community property is not separate property.

Date of Hearing: July 8, 1986

SB 1071ASSEMBLY COMMITTEE ON JUDICIARY
ELIHU M. HARRTS, Chairman

SB 1071 (Lockyer) - As Amended: July 13, 1986

PRIOR ACTION

Sen. Com. on JUD. 7-2

Sen. Floor 22-4

SUBJECT: This bill modifies the rights and responsibilities between spouses in the management and control of their community personal property.

DIGESTExisting law provides that:

- 1) A husband's and wife's earnings and accumulations acquired during marriage are their community property unless acquired as separate property. Their respective interests in the assets are present, existing, and equal.
- 2) As a general rule, either spouse has the management and control of the community property.
- 3) Each spouse must act in good faith with respect to the other spouse in that management and control.
- 4) A spouse may not sell, convey or encumber community personal property used as the family dwelling, or the furniture, furnishing, and clothing apparel without the written consent of the other spouse.
- 5) Both spouses must join in executing any instrument by which the community real property is leased for more than one year or is sold, conveyed, or encumbered.

This bill revises the law relating to management and control of community property to:

- 1) Provide that a spouse operating or managing a business or an interest in a business which is community property has the primary management and control of that business or interest. Primary management and control is defined as acting alone in conducting transactions in the normal course of business, with written notice given to the other spouse of any transaction which disposes of all or substantially all of the personal property used in the operation of a business.
- 2) Specify that each spouse shall act in good faith with respect to the other spouse in the management and control of the community property, continuing

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SB 1071

after separation until the court divides the property. The spouses are further required to make full disclosure to each other of the community assets and debts.

- 3) Provide that a spouse has a claim against the other spouse for a breach of a duty, as specified in (1) and (2) above, which results in substantial impairment.
- 4) Create other independent causes of action between spouses by permitting a spouse to request the court to (a) order an accounting of the parties' property and obligations; (b) determine ownership and use of the property; and (c) order that the name of a spouse be added to community property.
- 5) Provide a statute of limitations within which any of the above actions must be brought.
- 6) Provide a court procedure to dispense with a spouses' consent when such consent is necessary in a transaction. The court must determine that the transaction is in the best interests of the community and that the spouse has arbitrarily refused or is unable to consent.

FISCAL EFFECT

None

COMMENTS

- 1) According to the author, "existing law continues remnants of a societal policy that has perpetuated serious inequities in the management of community property." He states that this bill would go a long way toward updating and equalizing the rights of both spouses in this area.

According to the sponsor, the California Commission on the Status of Women, and cosponsor, the California Federation of Business and Professional Women, "this bill will ensure equal partnership marriages... It guarantees the participation of both spouses in the management and control of community property."

- 2) Legislative intent language states that this act is to clarify and enhance the duties owed by one spouse to another in managing community property. The Act is not to be interpreted or applied to adversely affect rights of any party under existing law other than a spouse.
- 3) Existing law requires spouses to act in good faith and in a reasonable manner with respect to the other spouse. It creates a marital fiduciary obligation between spouses which protects a person who is defrauded by

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his/her spouse. Case law has been strong in chastising spouses who have exercised undue influence over the other spouse thereby acquiring some financial advantage.

- 4) Proposed Section 5125(e) makes a significant change to the confidential relationship between spouses under existing law by extending a spouse's duty to disclose to the period of time during which a dissolution proceeding is pending. By so doing, this bill requires mandatory disclosure of assets between spouses in an adversarial proceeding and requires a spouse to make legal determinations as to the community or separate nature of property. An agent of the business spouse (e.g., a CPA or an attorney) may be placed into a trustee-like relationship with the other spouse, contrary to their professional ethics.

Should divorcing spouses be required to maintain a confidential or fiduciary relationship with each other?

Since information pertaining to community property is readily available upon demand, is this proposed extension of the duty between spouses necessary?

- 5) In a dissolution proceeding, the court may assess legal fees and costs of a spouse against the spouse with the better ability to pay. Since this bill amends the Family Law Act, the court would have the same discretion to award fees. A spouse who has sued for breach of duty may in fact be ordered to pay all fees and costs.

Should the attorney fees and costs be paid from the community resources, the award (if an award was sought) won by the injured spouse, or the separate property of the losing spouse?

Under the causes of action created by this bill, if a spouse wins a monetary award it is presumed to be community property by virtue of its acquisition during marriage. Should this award be treated as separate property?

- 6) Opponents have raised the following concerns:

- a) This bill, in effect, eliminates the protection provided by the "Innocent Spouse Rule" under tax law. Upon receipt of written notice, a spouse is essentially under a "duty" to take appropriate action and thus is no longer an "innocent spouse." [Also see comment 4 (a) (viii)]
- b) A spouse in business will be required to have a nuptial (marital) agreement in which the other spouse waives all her community property interest in the business.

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- c) Section 5125.1(c) should be amended to include "a general corporation, trust, or other type of business entity."

Otherwise, a title company may require a Quit Claim Deed from the noncontrolling spouse each and every time that a corporation, trust, or other entity takes title to business property when a married person is in control.

- d) This bill assumes that spouses can easily determine what property is community and what property is separate. Commingling occurs in many marriages. Should a spouse incur liability for good faith commingling?

Further, this bill once again raises the possibility of "pillow talk" discussions and other oral "agreements" being dragged into a courtroom, after recent legislative changes to have it excluded. Such duty to disclose under the trust law creates serious problems to the ability of a spouse to continue managing any business.

- e) The new potential actions between spouses in existing marriages will be detrimental to the continuity of families, and present an unreasonable intrusion of the court system into ongoing relationships.

Does the Legislature want the courts involved in intact marriages?

- f) This bill presents a significant risk that cases brought under the proposed Sections will be tied up in the appellate courts for years.

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