#F-3050/L-3050 ns80
10/24/91

Memorandum 91-62

Subject: Study F-3050/L-3050 - Nonprobate Transfers of Community Property (Comments on Tentative Recommendation)

The tentative recommendation relating to nonprobate transfers of community property was circulated to interested persons for comment in mid September, with comments requested by October 18. To date we have received four letters commenting on the tentative recommendation, copies of which are attached to this memorandum:

Exhibit 1 - Gregory Wilcox (Oakland)
Exhibit 2 - Melvin Wilson (Security Pacific Bank)
Exhibit 3 - Bob Temmerman (State Bar Estate Planning, Trust and Probate Law Section)
Exhibit 4 - Frieda Gordon Daugherty (Women Lawyers' Association of Los Angeles, Family Law Section)
Exhibit 5 - Joni S. Ackerman (Berverly Hills Bar Association, Probate, Trust & Estate Planning Legislative Committee)

Their comments are analyzed in staff notes inserted following the relevant sections in the attached copy of the tentative recommendation.

Our objective at this meeting is to make any necessary changes in the tentative recommendation and approve it for printing and submission to the 1992 legislature as a final recommendation.

Respectfully submitted,

Nathaniel Sterling
Executive Secretary

GREGORY WILCOX
ATTORNEY AT LAW

506 FIFTEENTH STREET, SUITE 700
OAKLAND, CALIFORNIA 94612-1486
(415) 451-2600
((510) after 9/2/91)

October 2, 1991

Nathaniel Sterling
California Law Revision Commission
4000 Middlefield Road, Room D2
Palo Alto, CA 94303-4739

Re: Nonprobate Transfers of Community Property

Dear Mr. Sterling:

Thank you for sending me the recent Tentative Recommendation relating to Nonprobate Transfers of Community Property, #F-3050/L-3050. I have enjoyed reading how you have handled the thorny issues in this area.

Many of the concerns I raised in my letter to you last year are resolved by the new suggested language. I am, however, still puzzled by way staff proposes to implement its intention to confirm that a married person may make a nonprobate transfer of the person's one-half interest in community property. The problem is best illustrated by the following hypothetical:

> A husband and wife have $100,000 in community property cash and no other assets. The husband puts $50,000 of this into a Totten Trust account naming his children by a former marriage as beneficiaries. The wife does not consent. Husband dies first, and wife wants to know what she can recover.

Your discussion approves of existing law, which you describe as providing for recovery of one-half of the community property gift on the death of the donor spouse, page 4. Likewise, the suggested language of §5021 states that the court may set aside a transfer as to the "nonconsenting spouse's interest in the property." The problem is that the extent of such "interest" is not clear.

The discussion seems to assume that the nonconsenting spouse's interest is one half of the asset subject to the nonprobate transfer. This is indeed a possible rule that one could adopt. However, if it is the rule, then nonprobate transfers are not really "will substitutes" as stated in the Comment to §5021.

One the one hand, it is absolutely clear under the authority of Probate Code §§101 and 6101 that if the husband in the example above had written a will leaving $50,000 to his children instead of using the Totten Trust, his children would be entitled to receive the entire $50,000 and his wife would have no claim to any of it. On the other hand, since he used a Totten Trust, current law gives the surviving spouse a claim to the return of one half, leaving the children with $25,000, and herself with $75,000. This latter result is exactly what is dictated by Estate of Wilson, 183 Cal. App. 3rd 67, 227 Cal. Rptr. 794 (1986).

Because the nonconsenting surviving spouse can recovery one half from nonprobate transfers, but cannot recover if the transfer is made by will, it is misleading to call such transfers "will substitutes."

Nevertheless, the Commission has done two things that seem to lead in the opposite direction. First, the language of §5021 and comment on page 4 introduce the idea that the surviving spouse should not be limited to recovery of the property itself, but rather be able to treat the property as fungible with other property or money, even that held in the other spouse's estate. However, if this is the approach, then all the property should be fungible, and there is no particular asset that the surviving spouse has any right to -- only his or her one half share of the total. Under this approach, the husband above should be able to give away the entire $50,000 in the Totten Trust accounts.

Second, staff Memorandum 90-109 squarely faced the issue of the community property interest subject to nonprobate transfer in a recommended new Probate Code §5001. This provision made it clear that a spouse could dispose of his or her one-half of the entire community property by nonprobate transfer. Surprisingly, however, this recommended section was deleted from the recent Tentative Recommendation, and §5001 reserved instead. Staff seems to have backed away from its earlier position, but only by negative implication.

It seems to me that whatever the result ought to be on this issue, this is the appropriate context in which to face and resolve it. Thank you again for this opportunity to comment on these matters.

Very truly yours,

GREGORY WILCOX

Memo 91-62

Office of the General Counsel
Head Office, Security Pacific Plaza
333 S. Hope Street, H23-80, Los Angeles, CA

P.O. Box 2097, H23-80
Los Angeles, California 90051

EXHIBIT 2

Study F-3050/L-3050
Law Revision Commission
RECEIVED
OCT 21 1991
File:
Key:

SECURITY PACIFIC BANK

Telephone (213) 345-8278 Facsimile (213) 345-3318

October 17, 1991

California Law Revision Commission
Suite D-2
4000 Middlefield Road
Palo Alto CA 94303-4739

F-3050/L-3050; Tentative Recommendation 9/17/91

Gentlemen:

This letter is in response to the Commission's request for comments on the Tentative Recommendations. Overall, we believe the staff, as usual, has put together an excellent solution.

Security Pacific has over a quarter of a million individual retirement accounts. From the introduction of IRAs in late 1974, the bank has used a form of beneficiary designation and spousal consent which is substantially identical to those used by the institutions involved in the Estate of MacDonald. The bank has a particular interest in remedial legislation which will obviate a global document replacement both because of the considerable expense of such program and because experience indicates that thousands of customers will fail to respond.

We approve of the approach outlined in the Tentative Recommendations and particularly agree with the concluding sentence of Recommendation 3 (p. 4) which states: "Disputes should be resolved among the interested parties and should not involve the neutral stakeholder."

However, we do have concerns as to the administrative feasibility of certain of the positions taken by the staff in the proposed curative legislation. These will be discussed within the framework of what we perceive to be the principal issues.

1 **Effect of death of consenting spouse, or, in the context of an IRA, can the surviving depositor spouse subsequently change the dispositive plan in the beneficiary designation form? This is the factual situation in MacDonald.**

We concur with the Commission's conclusion that, upon the death of the consenting nondepositor spouse, the consent should be viewed as a non-probate transfer which vests all incidents of ownership in the depositor spouse.

We believe that it is appropriate for the surviving depositor spouse to have the unrestricted right to modify the plan after the death of the consenting spouse because that seems consistent with the inferred intent of the spouses. When a consenting spouse consents to a dispositive plan which bypasses him or her, it is reasonable to infer that he or she understands and approves both the plan and the consequences of the consent. It is also reasonable to infer that the consenting spouse intends such waiver to become effective on his or her prior death and that the effect of such waiver is to confer on the surviving depositor spouse all of the incidents of ownership over the affected property.

2 **Effect of death of depositor spouse prior to the death of the consenting spouse, or, in the context of an IRA, can the surviving nondepositor spouse subsequently revoke the consent and thereby modify the dispositive plan?** This is the reverse of the factual situation in MacDonald. Suppose Mr. MacDonald had predeceased Mrs. MacDonald. Should she, or her personal representative, have had the right to modify or nullify Mr. MacDonald's dispositive plan?

If the nondepositor spouse consents to a dispositive plan which bypasses that spouse, it is reasonable to infer that the nondepositor spouse understands and approves the plan and the consequences of his or her consent. It is also reasonable to infer that the nondepositor spouse intends such consent to become effective on the death of the depositor spouse, even if that is prior to the death of the nondepositor spouse.

It is recognized that the Commission is attempting to incorporate in the statutory structure a distinction between writings which effect a transmutation immediately and those which postpone the transmutation until some determinable future time. The approach is carried into both Civil Code §5110.740 and Probate Code §5022 which provide that a spouse's consent will not constitute a transmutation unless the consent contains the bright line expression of intent required by CC §5110.730.

The problem with both sections is that they can be interpreted to mean that either they speak only at the time the consent is executed or they speak for all time. If a court adopts the latter interpretation, it could find that a consent which does not fully satisfy CC §5110.730 can never have the effect of a transmutation and that any attempt by Chapter 2 to effect a nonprobate transfer of the incidents of ownership through a consent is a nullity.

Although we believe the fail safe approach is to provide that when a consent becomes irrevocable it will have the effect of a transmutation, we recognize that the Commission may not wish to go that far. Assuming the Commission adopts the more conservative approach, we recommend that either the text of Civil Code §5110.740 and Probate Code §5022, or at least the legislatively endorsed Comments thereto, be modified so as to make it clear that those sections are intended to speak only as of the time of execution of a consent and that they shall not be construed to preclude a transmutation at the time a consent becomes irrevocable and operative under §5030.

Because of the rather stringent form over substance stance taken by the Supreme Court in MacDonald, we have a concern that a court might impose something as stringent as the CC §5110.730 "bright line" test for consents. It could be helpful to add to §5010 or the Comment thereto that a consent is not required to satisfy so stringent a test.

3 **Unilateral revocation of a spouse's consent, or, in the context of deposits accounts with financial institutions, third party claims.**

Proposed §5003(a) purports to relieve a financial institution from liability for a transfer which would prejudice the interest of a nondepositor spouse or other third parties. However, §5003(b) nullifies the protection to a financial institution which is provided by §5003(a) when the financial institution has received a written notice of an adverse claim.

Proposed §5012 purports to relieve the financial institution from any duty to resolve conflicting property right claims between spouses. Proposed §5031(b) purports to relieve the financial institution from liability if it transfers property in accordance with a dispositive plan to which a spouse has revoked his or her consent.

Proposed §5011 purports to allow a financial institution to regulate third party claims through appropriate provisions in the instrument establishing a deposit account. An example is a form of IRA beneficiary designation and spousal consent which expressly provides that the nondepositor spouse's consent can be revoked only by a new beneficiary designation executed by the depositor spouse, coupled with a new consent executed by the nondepositor spouse. Under §5011(a), such

procedure would nullify a written notice of revocation of the spouse's consent made in another form.

To summarize, the idea embodied in §5011(a) seems to that a financial institution can effectively insulate itself from the consequences of nonjudicial revocations of spousal consents and other forms of third party claims by appropriate provisions in the agreement s establishing deposit accounts, including IRAs. However, §5011 is susceptible to an interpretation which would nullify its intended effect.

The prefatory statement in §5011 limits its application to proposed Chapter 2. However, §5003, which is cross referenced by §§5012 and 5031, is in Chapter 1. Consequently, the safe harbor provided by §§5011(a), 5012 and 5031 could be construed to not apply to §5003. That means that a court may conclude that a spouse's consent can be unilaterally revoked by a separate writing. The court might also conclude that such revocation is effective even if delivered only to the depositor spouse as provided in §5031(a).

For those reasons, we recommend that the reference to "this chapter" in the prefatory statement in §5011 be amended to read "this part".

Very truly yours,

Melvin H. Wilson
Vice President & Associate Trust Counsel

cc P. Leahy
D. Lauer
M. Padden

ESTATE PLANNING, TRUST AND PROBATE LAW SECTION
THE STATE BAR OF CALIFORNIA

555 FRANKLIN STREET
SAN FRANCISCO, CA 94102
(415) 561-8289

REPLY TO: Robert E. Temmerman
Our File No. T-0977

October 21, 1991

Mr. Nathaniel Sterling, Esquire
California Law Revision Commission
4000 Middlefield Road, Suite D-2
Palo Alto, CA 94303-4739

Re: Tentative Recommendation Relating to Nonprobate Transfers of Community Property
Study # F-3050/L-3050

Dear Mr. Sterling:

In my letter dated September 10, 1991, I outlined comments and suggestions of Team 2 of the Estate Planning, Trust and Probate Law Section of the State Bar of California to Memorandum 91-53 which was the first draft of the tentative recommendation.

The suggestions of Team 2 as set forth in my September 10, 1991 letter was put to a vote of the Executive Committee of the Section on Monday, September 16, 1991. The Executive Committee of the Section concurred unanimously with the position of Team 2.

Since the meeting of the Section's Executive Committee, the Commission has circulated the Tentative Recommendation incorporating many of the proposed changes previously advanced by Team 2. On Wednesday, October 9, 1991, Team 2 held a two hour conference call concerning the Tentative Recommendation. Again, on Wednesday, October 16, 1991,

Team 2 had a follow up conference call lasting one hour. The participants in one or both of those conference calls included Elizabeth Engh, Irwin Goldring, Jim Hastings, Richard Konig, Valerie Merritt, Jim Quillinan, John C. Suttle, and myself.

The following comments to the Tentative Recommendations are those of Team 2 only as the full Executive Committee of the Section will not meet again until Saturday, October 26, 1991. If any revisions are made to the Team's Report, I will report on them orally at the next Law Revision Commission meeting scheduled for Friday, November 1, 1991 in Sacramento.

The following comments relate to the introduction and recommendation contained in Pages 1 through 8 of the Tentative Recommendation.

1. Page 2 - first full paragraph:

   The word "statutory" was most likely intended in lieu of the word "statute" in the first line of the first full paragraph.

2. Page 2 - footnote 6:

   The correct citation on the 9th Circuit Case of *Ablamis v. Roper* is 937 F2d 1450.

3. Page 3 - first paragraph:

   The cases of *Ablamis* and *McDonald* have caused concern not just in the estate planning bar but in the entire estate planning community, including plan administrator, trust companies, financial planners, and attorneys. Accordingly, Team 2 suggests replacing the word "bar" in the last sentence with the word "community".

4. Page 4 - last paragraph:

   Team 2 agrees that the Court should have discretion to fashion an appropriate remedy depending upon the circumstances of the case. However, Team 2 is of the opinion that there should be a suggested priority for recovery. For instance, a nonprobate transfer of community property made without consent unduly benefits the transferee. Accordingly, the Court should fashion a remedy that first looks to the transferee who has unduly benefitted from the transfer before resorting to other assets so as to fashion an equitable remedy. This issue will be discussed more fully in the proposed statute section 5021 set forth below. Team 2 suggests modifying the second to the last sentence in this paragraph to read as follows: "Likewise the spouse should be able to proceed against the donor's estate in addition to proceeding against the beneficiary of the nonprobate transfer."

5. Page 6 and 7 - Effect of Death of Consenting Spouse:

Team 2 and now the full Executive Committee of the Estate Planning, Trust and Probate Law Section of the State Bar of California concurs in the approach taken by the Law Revision Commission regarding the interim period between the death of the consenting spouse and the death of the donor spouse. The Executive Committee of the State Bar is of the opinion that the surviving spouse should be able to deal with only that spouse's share of the community property, but not the consenting spouse's share of the community property. After the death of the consenting spouse, the best indication of the decedent's intent is as indicated on the beneficiary designation or other nonprobate transfer of property. Thus, the decedent's consent to a beneficiary designation becomes frozen at his or her death, unless there is an agreement enabling the surviving spouse to make controlling decisions as to a change in beneficiaries over both halves of the community property.

The following comments relating to the proposed statutes and comments governing nonprobate transfers of community property beginning at page 9 of the Tentative Recommendation.

1. Page 11 - §5003:

One articulate and vocal member of Team 2 would prefer a statute that imposes more liability on the holders of the property. He reasoned that the holders of the property are paid fees and that they should have some responsibility to ensure that consents get signed. The majority of Team 2 believed that it was not an onerous burden to provide written notice to the holder claiming an adverse interest in the property. Accordingly, the statute as drafted was favored by Team 2.

2. Page 13 - §5011, comment:

Insert the correct cite for *Ablamis v. Roper* as 937 F2d 1450.

3. Page 15 - §5021:

The Commission recommends that for nonprobate transfers of community property made without consent, the Court should have discretion to fashion an appropriate remedy depending upon the circumstances of the case. Team 2 discussed whether or not the statute should provide guidance to the Court regarding the priority of recovery. For instance, Team 2 believed that in most cases it would be more equitable to proceed against the beneficiary of the nonprobate transfer who has possession of the property rather than against the transferor's estate or living trust which may indeed be for the benefit of beneficiaries other than the transferee of the nonprobate transfer. Accordingly, Team 2 suggest that the Court should fashion a remedy that first resorts to the property in the hands of the transferee but if it is not recoverable, then against the transferror other community assets whether governed

by a will, living trust, or other nonprobate transfer. Team 2 firmly believes that the Court is in the best position to take into account the rights of all interested parties. Team 2 suggests that even if the Commission should not concur in the suggested priority of remedies, that it should at least consider modifying subdivision (b) to read as follows:

> (b) Nothing in subdivision (a) of this section affects any additional remedy the nonconsenting spouse may have against the person's estate for a nonprobate transfer of community property on death without the spouse's written consent.

4. Page 15 - §5021, comment:

If Subdivision (b) is modified as set forth above, the comment regarding Subdivision (b) (third paragraph) should be modified for consistency. For instance, the second sentence of the third paragraph in the comment might read as follows: "It may be proper, for example and without limitation, simply to allow the surviving spouse instead of or in addition to proceeding against the beneficiary of the nonprobate asset to also proceed against the decedent's estate for an offset of the value of the property transferred out of the share of the decedent, or to give the surviving spouse a right or reimbursement."

If the Commission adopts any sort or priority approach as far as the available remedies are concerned, corresponding changes should be made at page 4 of the introduction and recommendations.

5. Page 16 - §5023:

Team 2 strongly agrees with the approach taken by the Law Revision Commission concerning the effect of modification after the consenting spouse's death. As previously noted, the Executive Committee of the State Bar Section on Estate Planning, Trust and Probate Law has voted unanimously in support of this position.

Team 2 is in favor of the approach taken by the Commission in paragraph (3) of subdivision (b). Team 2 does suggest however inserting the word "the" after the word "after" and before the word "spouse's" in line 4 of that paragraph. Further, paragraph (3) of subdivision (b) provides the opportunity for a spouse to leave the surviving spouse with a general power of appointment over the property. There were some concern among the members of Team 2 that perhaps any forms that might be developed to accommodate the result contemplated might incorporate some warning language. For instance, a general power of appointment may trigger a significant economic shift and some severe tax consequences to the holder of the power. Perhaps some warning language suggesting that the parties should seek legal or tax advice before executing what is in effect a general power of appointment might be warranted.

6. Pages 17 and 18 - §5030:

In order to be consistent with §5023 (b) (3), subdivision (c) should be modified and a subdivision (d) should be added to read as follows:

> (c) On the death of the transferor spouse, the written consent is irrevocable.
>
> (d) On the death of the consenting spouse, the written consent is governed by §5023 above.

7. Page 18 - §5030, Comment:

A new second paragraph should be added to read "Subdivision (c) continues existing law."

The present second paragraph should become the third paragraph and would read correctly if it referred to subdivision (d) instead of (c) and omitted the words "to the extent it relates to the death of the consenting spouse". The paragraph should also contain a sentence that might read as follows: "Section 5023 (b) allows the surviving spouse to modify the provisions for the transfer of nonprobate property if the deceased consenting spouse has so indicated as a part of the original consent."

8. Page 18, §5031:

This section deals with the concept of revocation of a consent that has been previously given for a nonprobate transfer of community property. Page 5 of the introduction of the tentative recommendation wisely states that "[r]evocation should not be effective unless the other spouse is informed (emphasis added) of the revocation before death . . ." The introduction states the rational for this provision: ". . . this will ensure that any corresponding changes in the spouse's estate plan necessitated by the revocation can be made." Team 2 suggests that these provisions on revocation of consent be codified and added to the statute.

Team 2 agrees that the other spouse should have an opportunity to make corresponding changes in his or her estate planning.

Subdivision (a) provides that "the consenting spouse may revoke the consent by a writing . . . that is delivered to the married person before the married person's death." Team 2 believes that mere delivery should not be enough. The revocation should only be effective if it is delivered under circumstances which allow the married person a reasonable opportunity to make corresponding changes in that person's estate planning which may be required as a result of the revocation. Thus, the concept of delivery would be modified to allow the Court to take into consideration circumstances that would allow the recipient spouse a reasonable

opportunity to make appropriate changes in his or her estate plan. Such a requirement would provide for an element of fairness. For instance, if the recipient of the delivered notice is comatose, mentally disabled, or otherwise unable to respond, the revocation would be ineffective until such time as the incapacitated person has a reasonable opportunity to make changes in his or her estate planning through a substituted judgment proceeding or by an agent under a Durable Power of Attorney.

Team 2 recognizes that its "reasonable opportunity" approach may create significant litigation over the more "cut and dry" concept of delivery. Despite such difficulty however, Team 2 advocates a drafting solution which turns the concept of "delivery" of a notice of revocation of consent from a less mechanical concept into one based upon fundamental fairness.

I am a member of Team 2 and plan on being at the next meeting of the Law Revision Commission on Friday, November 1, 1991 should any clarification of our views as expressed herein be desired.

Sincerely,

Robert E. Temmerman, Jr.
Team 2 Captain
RET/gmd (ster1017.let)

cc: Members of Team 2 (by mail)
Members of the Executive Committee (by handout at Executive Committee Meeting)
Monica Dell O'sso (ExComm's LRC Representative)
Tom Strikker (ExComm's LRC Representative)

LAW OFFICES OF
FRIEDA GORDON DAUGHERTY

433 NORTH CAMDEN DRIVE · SUITE 1111 · BEVERLY HILLS, CA 90210
TELEPHONE (213) 275-1554 · (213) 275-1584 · FAX (213) 858-1226

FRIEDA GORDON DAUGHERTY*
*CERTIFIED FAMILY LAW SPECIALIST

October 21, 1991

CALIFORNIA LAW REVISION COMMISSION
4000 Middlefield Road, Suite D-2
Palo Alto, California 94303-4739

Attention Nathaniel Sterling

Re: California Law Revision Commission;
Donative Transfers of Community Property

Dear People:

I have had the opportunity to review your proposed legislation and have particular interest in working with the Commission in successfully passing a bill overturning the current law as was held in the Estate of McDonald. I am also a Certified Family Law Specialist and Chairman of the Family Law Section of Woman Lawyers' Association of Los Angeles. In that capacity I co-authored an amicus brief supporting the respondent Friedman, Sloane and Ross in Droeger v. Friedman, Sloane and Ross, which case recently upheld the Court of Appeal ruling which voided a note secured by deed of trust on a parcel of community property which transaction did not have the other spouse's written consent.

I am planning to attend the October 31st meeting of your organization in Sacramento on behalf of the Legislative Committee of the Probate, Trust and Estate Planning Section of the Beverly Hills Bar Association and I am requesting as an individual that the following issues be addressed:

1. Whether the designation of beneficiaries ought to address the contingency of death occuring during the pendency of divorce.

2. Whether the fact that at the last minute at the State Bar Conference Of Delegates a resolution was passed to overrule Droeger and codify the law that a spouse may encumber or transfer up to his or her one-half interest in any piece of community property without the written consent of the non-consenting spouse, provided notice is given to that spouse within a specified period of time should impact the course and scope of the proposed bill regarding donative intent.

I believe that it would be both time and cost-efficient if the problems that arose from the ruling in Droeger could be solved concurrently with the problems that arose with the ruling in the Estate of McDonald, since they address the same basic issue, the issue of consent relative to the transfer of community property. The combining or tracking of the two bills will avoid potential conflict with the Probate and Civil Codes. Thus it would be easier to inform the public of the common changes.

I look forward to working with you on these issues at the upcoming meeting of the Law Revision Commission and sincerely thank you for your time and effort in resolving this particularly confusing area of law.

Very truly yours,

FRIEDA GORDON DAUGHERTY
Certified Family Law Specialist

FGD:ccp
cc: Joni S. Ackerman, Esq.
Lisa Alexander, Esq.
Jeffrey A. Altman, Esq.
Janice Fogg, Esq.
Phyllis Cardoza
LET\LAW-REV.LTR

LAW OFFICE OF
JONI S. ACKERMAN
WORLD SAVINGS BUILDING
1901 WILSHIRE BOULEVARD, SUITE 2100
LOS ANGELES, CALIFORNIA 90026
TELEPHONE (213) 975-3035
FACSIMILE (213) 975-3033

Via Facsimile

October 24, 1991

California Law Revision Commission
4000 Middlefield Road, Suite D-2
Palo Alto, CA 94303-4739

Attn: Nathanial Sterling

Re: Study L-3050 -- Donative Transfers of Community Property

Dear Mr. Sterling:

On behalf of the Beverly Hills Bar Association, Probate, Trust & Estate Planning Section's Probate Legislative Committee ("Committee"), this letter is to respond to the most recently circulated papers and the Commission's position with regard to the above-referenced study.

Our Committee supports the position of the Commission that a surviving spouse should only be able to alter a designation of beneficiary as to the surviving spouse's one-half interest in the asset in question, after the death of the decedent spouse. This follows the usual community property default rule that a person may only effect disposition as to his or her one-half of the community property. We agree that the decedent spouse's interest in the asset in question and the designation of beneficiary for that asset may not be modified, amended or altered by the surviving spouse after the decedent spouse has died.

Our Committee supports the position of the Commission that the surviving spouse may only effect a change to the decedent spouse's interest in, and designation of beneficiary for, a community property asset where the decedent spouse gave the surviving spouse a power of appointment which specifically refers to the surviving spouse's power over the asset in question.

Our Committee supports the Commission's position that revocation of a spouse's consent to a designation of beneficiary may be effected by the delivery of a writing delivered to the other spouse. However, our Committee has concerns regarding the retroactivity of

such an action, where, as in the Estate of MacDonald, a property agreement has been entered into by the spouses, and a retroactive revocation of consent by the decedent spouse would adversely affect such an agreement. Our Committee supports the position that such a revocation may be made by a spouse in a writing that is delivered to the other spouse during both spouses' lifetimes, and not after or as a result of the death of a spouse.

Respectfully Submitted,

Joni S. Ackerman
Chair, Probate Legislative Committee
of the Probate, Trust & Estate
Planning Section of the Beverly
Hills Bar Association

JSA:aj

cc: Lisa Alexander
Jeffrey Altman
Phyllis Cardoza
Frieda Daugherty
Janice Fogg

#F-3050/L-3050 ns52

TENTATIVE RECOMMENDATION

relating to

NONPROBATE TRANSFERS OF COMMUNITY PROPERTY

INTRODUCTION

A married person may dispose of the person's one-half interest in community property[1] by will or by nontestamentary transfer effective at death.[2] Case law has extended the statutory limitation on lifetime gifts of community property[3] to donative transfers at death: A married person may not make a transfer of community property effective at death without the written consent of the person's spouse; after the death of the transferor, a donative transfer made without the required consent

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1. See Prob. Code § 100. A married person may also make a testamentary disposition of the person's interest in the person's quasi-community property. See Prob. Code § 101. This recommendation does not deal with a nonprobate transfer of quasi-community property, however, since such a transfer may present different policy considerations. The Commission has reserved this matter for future review.

2. While the ability of a married person to will the property is statutory (Prob. Code § 6101), to determine the existing law on nonprobate transfers requires both a close reading of the statutes and a knowledge of the cases. See, e.g., Tyre v. Aetna Life Ins. Co., 54 Cal. 2d 399, 353 P.2d 725, 6 Cal. Rptr. 13 (1960) (beneficiary designation in community property life insurance policy); Estate of Wilson, 183 Cal. App. 3d 67, 227 Cal. Rptr. 794 (1986) (Totten Trust account for benefit of third party).

So fundamental a principle--that a married person may make a nonprobate transfer of the person's one-half interest in community property--should be clear, and the Commission's recommendations on nonprobate transfers of community property will have the incidental effect of clarifying the matter.

3. Civ. Code § 5125(b) ("A spouse may not make a gift of community personal property, or dispose of community personal property without a valuable consideration, without the written consent of the other spouse.").

may be set aside as to the one-half interest of the nonconsenting spouse.[4]

This rudimentary framework of ~~statute~~ statutory and case law governing nonprobate transfers of community property has proved to be inadequate to handle this increasingly important area of law. Typical problems are revealed in two recent cases--*Estate of MacDonald*[5] in the California Supreme Court and *Ablamis v. Roper*[6] in the United States Court of Appeals for the Ninth Circuit.

MacDonald involved a husband who moved community property from an employee pension plan to an Individual Retirement Account (IRA), naming as beneficiary under the IRA a trust for his children from a former marriage. The wife signed a written consent to the beneficiary designation, but after her death and while her husband was still alive her personal representative revoked the consent and sought to recover the wife's one-half interest in the community property for the wife's estate. The California Supreme Court held that the wife's consent to a beneficiary designation was not a transmutation of the wife's interest in the community property into the husband's separate property, with the result that the consent remained revocable and the revocation could be exercised after the wife's death by her personal representative.

Ablamis also involved a wife's interest in her husband's community property pension plans. In that case the wife did not consent to any particular disposition of the property, and died leaving her interest in community property to a trust for her children of a former marriage. When the wife's personal representative claimed a one-half interest in each of the husband's pension plans, the United States Court of Appeals (9th Circuit) held that the federal Employee Retirement Income Security Act of 1974 (ERISA) preempts state community

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4. See, e.g., Travelers' Insurance Co. v. Fancher, 219 Cal. 351, 26 P. 2d 482 (1933) and Blethen v. Pacific Mutual Life Insurance Co., 198 Cal. 21, 243 P. 431 (1926) (beneficiary designation under life insurance policy); Estate of Wilson, 183 Cal. App. 3d 67, 227 Cal. Rptr. 794 (1986) (Totten trust accounts).

5. 51 Cal. 3d 262, 794 P.2d 911, 272 Cal. Rptr. 153 (1990).

6. ~~___ F.2d ___ (9th Cir. 1991) (89-15352)~~ 937 F.2d 1450 (9th Cir. 1991).

property laws and precludes the wife's estate from asserting its interest in the community property pensions.

These cases illustrate a paradox in the law governing this area: The wife's estate in *MacDonald* could recover the wife's community property interest despite the wife's consent to the husband's disposition, whereas the wife's estate in *Ablamis* could not recover the wife's community property interest even though the husband's disposition was made without the wife's consent. The cases also demonstrate both the confusion in the law over the relevant legal principles that control a nonprobate transfer of community property and a spousal consent to a transfer, and the need for statutory clarification. The cases have caused consternation in the estate planning ~~bar~~ community over the inability of a spouse to make a coherent estate plan using standard nonprobate transfer techniques with any assurance that the law will honor the proposed disposition.

RECOMMENDATIONS

The California Law Revision Commission recommends codification of the general principles governing nonprobate transfers of community property. This is an area of law that is assuming major importance as increasing amounts of wealth are passed through nonprobate devices such as beneficiary designations in employee benefit plans, life insurance policies, living trusts, multiple party bank accounts, and the like.[7] The law has not caught up with practice in the area, and cases have developed on a piecemeal and inconsistent basis. Codification of the general principles will benefit both practitioners and the courts in dealing with this area of law.

The Commission has adhered to the following general principles in developing specific recommendations for legislation to govern nonprobate transfers of community property:

(1) As an equal owner of community property, each spouse should have an equal right to control disposition of half the property at death.

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7. Typical nonprobate transfer devices are cataloged in Probate Code Section 5000.

(2) A spouse's written expression of intent should control over contrary statutory default rules governing disposition of a spouse's interest in community property at death.

(3) A third party acting under the terms of a nonprobate transfer instrument should be protected in making the transfer notwithstanding the existence of contrary rights in the property. Thus, for example, a pension plan trustee may make a transfer under the terms of the plan, whether or not the transfer corresponds to community property rights of spouses and beneficiaries. Disputes should be resolved among the interested parties and should not involve the neutral stakeholder.

Spousal Consent Requirement

Existing case law recognizes that a nonprobate transfer of community property at death is a donative transfer, and as such treats it in a manner similar to a gift of community property.[8] The Commission recommends express codification of the gift rule for nonprobate transfers of community property. Thus a donative transfer of community property is voidable as to the one-half interest of the donor's spouse if made without the written consent of the spouse.

While existing law governing gifts provides for recovery of one-half of the community property gift on the death of a spouse, this remedy is unduly restrictive. The Commission recommends that for nonprobate transfers of community property made without consent, the court should have discretion to fashion an appropriate remedy, depending on the circumstances of the case. The court may, for example, order return of the value of the property instead of the property itself, or may order return of a particular item of property while allowing an item of offsetting value to pass. Likewise, the spouse should be able to proceed against the donor's estate ~~rather than~~ in addition to proceeding against the beneficiary of the nonprobate transfer. It may be proper, for example, simply to allow the surviving spouse a setoff for the value of the property transferred out of the share of the decedent or to give the surviving spouse a reimbursement right.

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8. See discussion at notes 3 and 4, above.

Effect of Consent

The *MacDonald* case points out that a spousal consent to a nonprobate transfer of community property does not transmute the consenting spouse's community interest into separate property of the other spouse. A person who consents to a particular disposition of community property on death of the persons's spouse is consenting only to its disposition at death. Until then, the property retains its community character and is subject to all incidents of community property, including division at dissolution of marriage. This rule should be codified, but would not preclude a spouse from making a transmutation of community property if so desired by an express declaration of intent.[9]

Since a nonprobate transfer of community property, like a will, is not intended to take effect until death, it should remain revocable until that time.[10] To impose some structure on the revocation process and because the original consent is in writing, a consent should only be revocable in writing. Revocation should not be effective unless the other spouse is informed of the revocation before death; this will ensure that any corresponding changes in the spouse's estate plan necessitated by the revocation can be made.[11]

After the donor spouse dies, the ability of the consenting spouse to revoke and make a different disposition of the community property

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9. See Civ. Code § 5110.730(a) ("A transmutation of real or personal property is not valid unless made in writing by an express declaration that is made, joined, consented to, or accepted by the spouse whose interest in the property is adversely affected.").

10. This rule would not apply to a consent that by its terms is irrevocable.

11. Where the written revocation is made in the consenting spouse's will, the additional requirement should be imposed that the will is admitted to probate before the death of the other spouse. This replaces the delivery requirement: It ensures that the revocation contained in the will is the consenting spouse's last word on the matter, and that the other spouse receives notice (through the estate administration process).

should terminate. The donative transfer has become a completed gift at this point, beyond the spouses' power to change.

Effect of Death of Consenting Spouse

The most difficult issues involve the situation presented in *MacDonald*--rights among the parties after the death of the consenting spouse but before the death of the donor spouse. May the consenting spouse's successors revoke the consent before the nonprobate transfer becomes a completed gift? May the donor spouse make changes in the terms of the gift that conflict with the terms consented to by the deceased spouse?

The court in *MacDonald* did not reach the issue of exercise of the revocation right by the consenting spouse's personal representative after the consenting spouse's death. The Commission believes the consent of a spouse to a nonprobate transfer of community property is itself a nonprobate transfer, and should become irrevocable on the death of the consenting spouse. The consenting spouse's successors should not, after the spouse's death, be permitted to undo the decedent's estate plan for their own benefit. The recommended law would honor the clearly expressed written intent of the deceased spouse with respect to disposition of the decedent's interest in the community property.

During the interim period between the death of the consenting spouse and the death of the donor spouse, the donor spouse may seek to change the terms of the proposed nonprobate transfer, for example by designating a different beneficiary or by revoking the transfer in whole or in part. In this case, the Commission recommends that the law recognize the authority of the surviving spouse to deal with and dispose of the survivor's half of the community property, but not the decedent's half. The deceased spouse is no longer able to give consent to changed terms,[12] and therefor the decedent's half should pass in

12. If the donor spouse makes a change in terms during the lifetime of the consenting spouse, on the other hand, the consenting spouse is in a position to respond. In this situation the proposed law provides that the change in terms revokes the consent, unless the consenting spouse gives further consent to the changed terms.

accordance with the decedent's last expressed intent, as indicated in the consent to the nonprobate transfer. This has the effect of preserving the right of the deceased spouse to control ~~dispostion~~ disposition of the decedent's one-half interest in the community property on the decedent's death.

It should be noted, however, that the surviving spouse may be in a position to judge the needs of potential beneficiaries as circumstances change in the interim period after the death of the first spouse to die. For this reason the proposed law recognizes that the spouses may determine ahead of time that by consenting to or joining in a nonprobate transfer, the spouses express confidence in the survivor to make appropriate changes in the disposition of both halves of the community property. Statutory recognition of such an agreement will enable the spouses to allow the survivor to make controlling decisions, in place of the statutory default rule that freezes the terms of the proposed disposition of the decedent's interest on death.

Note. The Law Revision Commission particularly solicits comments on the issues raised concerning the ability of the surviving spouse to make changes in a previously consented to provision for a nonprobate transfer on death.

Federal Preemption

The Commission recommends enactment of the foregoing principles as part of California law. However, it is clear from the *Ablamis* case that the California rule permitting a nonemployee spouse to make a separate disposition of a one-half interest in a community property pension plan may not be applied to employee pension plans under ERISA.[13] The Commission plans to give this matter further review.

Retroactivity

Before *MacDonald*, a person who executed a consent to a nonprobate transfer of community property would ordinarily have assumed that the consent would dispose of the person's interest in the community in the

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13. See ~~29 U.S.C. § 1056(d) (19--)~~ 29 U.S.C.A. § 1056(d) (Supp. 1991) (assignment or alienation of benefits under a covered retirement plan precluded).

manner consented to. Such a consent should be saved to the greatest extent possible, and an estate plan should not be destroyed by allowing the heirs of the consenting spouse to overturn it after the spouse's death. For this reason the Commission recommends that codification of the law governing nonprobate transfers of community property should also be applied to a spousal consent executed before the operative date of the codification.

Retroactive operation would be subject to an exception that where the consenting spouse died before the operative date of the codification, former law continues to apply. This would preserve rights of the decedent's successors that may have vested under the *MacDonald* doctrine and cannot constitutionally be disturbed.[14]

Staff Note. The changes in the text above marked in strikeout and underscore are suggested by State Bar Team 1. The staff would make these changes.

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14. Cf. *In re* Marriage of Buol, 39 Cal. 3d 751, 705 P. 2d 354, 218 Cal. Rptr. 31 (1985) and *In re* Marriage of Fabian, 41 Cal. 3d 440, 715 P. 2d 253, 224 Cal. Rptr. 333 (1986) (constitutional limitation on retroactive operation of Civil Code §§ 4800.1 and 4800.2).

OUTLINE

PROBATE CODE

DIVISION 5. NONPROBATE TRANSFERS

PART 1. PROVISIONS RELATING TO EFFECT OF DEATH

CHAPTER 1. GENERAL PROVISIONS

§ 5000. Nonprobate transfer at death
§ 5001. [Reserved for future use]
§ 5002. Limitations imposed by instrument
§ 5003. Protection of holder of property

CHAPTER 2. NONPROBATE TRANSFERS OF COMMUNITY PROPERTY

Article 1. General Provisions
§ 5010. "Written consent" defined
§ 5011. Governing provision of instrument, law, or consent
§ 5012. Community property rights independent of transfer obligation
§ 5013. Waiver of rights in community property
§ 5014. Transitional provision

Article 2. Consent to Nonprobate Transfer
§ 5020. Written consent required
§ 5021. Transfer without written consent
§ 5022. Written consent not a transmutation
§ 5023. Effect of modification

Article 3. Revocation of Consent
§ 5030. Revocability of written consent
§ 5031. Form and delivery of revocation
§ 5032. Effect of revocation

CONFORMING CHANGES

Civ. Code § 5110.740 (amended). Estate planning documents
Prob. Code § 141 (amended). Rights that may be waived

PART 1. PROVISIONS RELATING TO EFFECT OF DEATH

SEC. . A chapter heading is added to Part 1 (immediately preceding Section 5000) of Division 5 of the Probate Code, to read:

CHAPTER 1. GENERAL PROVISIONS

Prob. Code § 5000 (unchanged). Nonprobate transfer at death

5000. (a) A provision for a nonprobate transfer on death in an insurance policy, contract of employment, bond, mortgage, promissory note, certificated or uncertificated security, account agreement, custodial agreement, deposit agreement, compensation plan, pension plan, individual retirement plan, employee benefit plan, trust, conveyance, deed of gift, marital property agreement, or other written instrument of a similar nature is not invalid because the instrument does not comply with the requirements for execution of a will, and this code does not invalidate the instrument.

(b) Included within subdivision (a) are the following:

(1) A written provision that money or other benefits due to, controlled by, or owned by a decedent before death shall be paid after the decedent's death to a person whom the decedent designates either in the instrument or in a separate writing, including a will, executed either before or at the same time as the instrument, or later.

(2) A written provision that money due or to become due under the instrument shall cease to be payable in event of the death of the promisee or the promisor before payment or demand.

(3) A written provision that any property controlled by or owned by the decedent before death that is the subject of the instrument shall pass to a person whom the decedent designates either in the instrument or in a separate writing, including a will, executed either before or at the same time as the instrument, or later.

(c) Nothing in this section limits the rights of creditors under any other law.

Comment. Section 5000 is intended broadly to validate written instruments that provide for nonprobate transfers on death. The listing in the section of types of written instruments is not exclusive, and the section also would validate, for example, a nonprobate transfer provision in a partnership agreement, stock redemption plan, buy-sell agreement, power of appointment, and the like.

Staff Note. Section 5000 is unchanged. It is set out here for convenience of reference, together with a supplementary comment.

Prob. Code § 5001 (Reserved for future use).

Prob. Code § 5002 (added). Limitations imposed by instrument

SEC. . Section 5002 is added to the Probate Code, to read:

5002. Notwithstanding any other provision of this part, a holder of property under an instrument of a type described in Section 5000 is not required to receive, hold, or transfer the property in compliance with a provision for a nonprobate transfer on death executed by a person who has an interest in the property if either (1) the person is not authorized by the terms of the instrument to execute a provision for transfer of the property, or (2) the provision for transfer of the property does not otherwise satisfy the terms of the instrument.

Comment. Section 5002 is added to make clear that this part is not a substantive grant of authority for a person to enforce a nonprobate transfer of the person's interest in property where such a transfer is not authorized by the terms of the instrument under which the property is held. Thus, for example, a nonemployee spouse under an employee benefit plan, or a nonowner spouse under an insurance policy, is not authorized by this part to direct a nonprobate transfer of the spouse's community property interest, if any, in the plan or policy. Although this chapter does not authorize execution of a provision for such a nonprobate transfer, the holder of the property may be required by federal law, by other state law, or by the terms of the instrument itself to recognize the property interest of a spouse.

Prob. Code § 5003 (added). Protection of holder of property

SEC. . Section 5003 is added to the Probate Code, to read:

5003. (a) A holder of property under an instrument of a type described in Section 5000 may transfer the property in compliance with a provision for a nonprobate transfer on death that satisfies the terms of the instrument, whether or not the transfer is consistent with the beneficial ownership of the property as between the person who executed the provision for transfer of the property and other persons having an interest in the property or their successors.

(b) Except as provided in this subdivision, no notice or other information shown to have been available to the holder of the property affects the right of the holder to the protection provided by subdivision (a). The protection provided by subdivision (a) does not extend to a transfer made after the holder of the property has been served with a contrary court order or with a written notice of a person claiming an adverse interest in the property.

(c) The protection provided by this section does not affect the rights of the person who executed the provision for transfer of the property and other persons having an interest in the property or their successors in disputes among themselves concerning the beneficial ownership of the property.

(d) The protection provided by this section is not exclusive of any protection provided the holder of the property by any other provision of law.

Comment. Section 5003 is drawn from portions of Section 5405 (protection of financial institution under California Multiple-Party Accounts Law); see also Health & Safety Code § 18102.3; Veh. Code §§ 5910.7, 9916.7 [SB 271]. A holder of property that is the subject of a nonprobate transfer is not obligated to ascertain the respective separate, community, and quasi-community property interests in the property of participant and nonparticipant, or employee and nonemployee, or covered and noncovered, or insured and noninsured, spouses. Unless the holder of property has been served with a contrary court order or notice of an adverse claim, the holder may transfer the property in accordance with the terms of the instrument, and any adverse rights of a spouse or beneficiaries must be asserted against the estate of the person who executed the instrument or against the beneficiary, not against the holder of the property. See Sections 5012 (community property rights independent of transfer obligation), 5021 (transfer without consent).

Staff Note. State Bar Team 2 supports this section as drafted, but notes that one member of the team would prefer a statute that imposes more liability on holders of property, reasoning that the holders are paid fees and should have some responsibility to ensure that consents get signed.

The staff does not believe the protection given neutral stakeholders should be changed. To begin with, many holders of property for nonprobate transfer are uncompensated. In addition, the mere fact that there is a consent on file does not resolve the problem, since there may be revocations of consent, etc., of which the property holder is unaware; as Team 2 points out, it is not an onerous burden to provide written notice to the holder claiming an adverse interest in the property. And, as a practical matter, if we wish to get legislation enacted the protection for banks and other holders must be in place.

Prob. Code §§ 5010-5032 (added). Nonprobate transfers of community property

SEC. . Chapter 2 (commencing with Section 5010) is added to Part 1 of Division 5 of the Probate Code, to read:

CHAPTER 2. NONPROBATE TRANSFERS OF COMMUNITY PROPERTY

Article 1. General Provisions

§ 5010. "Written consent" defined

5010. As used in this chapter, "written consent" to a provision for a nonprobate transfer of community property on death includes a written joinder in such a provision.

Comment. Section 5010 is intended for drafting convenience. Written joinder in a provision for a nonprobate transfer includes joint action by both spouses in writing. A written consent, to be effective, need not satisfy the statutory requirements for a transmutation. See Section 5022 (written consent not a transmutation). A written consent becomes irrevocable on death of either spouse. Section 5030 (revocability of written consent).

Staff Note. We have augmented the Comment in response to a suggestion by Melvin Wilson of Security Pacific Bank.

§ 5011. Governing provision of instrument, law, or consent

5011. Notwithstanding any other provision of this ~~chapter,~~ part, the rights of the parties in a nonprobate transfer of community property on death ~~is governed by~~ are subject to all of the following:

(a) The terms of the instrument under which the nonprobate transfer is made.

(b) A contrary state statute specifically applicable to the instrument under which the nonprobate transfer is made.

(c) A written expression of intent of a party in the provision for transfer of the property or in a written consent to the provision.

Comment. Section 5011 establishes the principle that the rules in this chapter only apply in the absence of other governing provisions.

Subdivision (a) recognizes that the terms of the instrument may define the rights of the parties. See also Section 5012 (community property rights independent of transfer obligation).

Subdivision (b) makes clear that the general rules set out in this chapter are not intended to override other state statutes that are narrowly drawn to govern rights under specific named instruments. It should also be noted that this chapter cannot override preempting federal law. See, e.g., Ablamis v. Roper, ~~___ F.2d ___ (9th Cir. 1991) (No. 89-15352)~~ 937 F.2d 1450 (9th Cir. 1991) (ERISA precludes testamentary disposition of community property interest of nonparticipant spouse).

Subdivision (c) makes clear that an expression of intent of the spouses in directing a nonprobate transfer of their interests in community property prevails over the default rules in this chapter.

Staff Note. The staff has changed the reference from "chapter" to "part" in response to the point made by Melvin Wilson of Security Pacific Bank that the terms of an account may require execution of a special form before the bank gives effect to a change of beneficiaries. This should override Section 5003, which is located in Chapter 1 of this Part; that section nullifies the bank's immunity when it receives any type of written adverse notice.

But Mr. Wilson's point also demonstrates that Section 5011 is too broadly drawn, since the section seems to say that the bank and its depositor can by agreement override anything contrary, including a court order. All we really intend by Section 5011 is that the rights of parties to a nonprobate instrument are subject to such matters as the terms of the instrument and expressions of intent of the parties. This interpretation is already reflected in the Comment to the section, and we have narrowed the draft statutory language accordingly to help avoid an overly broad interpretation of the section.

§ 5012. Community property rights independent of transfer obligation

5012. A provision of this chapter concerning rights between a married person and the person's spouse in community property is relevant only to controversies between the person and spouse and their successors and does not affect the obligation of a holder of community property under an instrument of a type described in Section 5000 to hold, receive, or transfer the property in compliance with a provision for a nonprobate transfer on death, or the protection provided the holder by Section 5003.

Comment. Section 5012 is drawn from Section 5201 (multiple-party accounts).

§ 5013. Waiver of rights in community property

5013. Nothing in this chapter limits the effect of a surviving spouse's waiver of rights in community property under Chapter 1 (commencing with Section 140) of Part 3 of Division 2.

Comment. Section 5013 recognizes an alternate procedure for releasing rights of a surviving spouse in community property.

Waiver of a joint and survivor annuity or survivor's benefits under the federal Retirement Equity Act of 1984 is not a transmutation. Civil Code § 5110.740 (estate planning instruments).

§ 5014. Transitional provision

5014. (a) Except as provided in subdivision (b), this chapter applies to a provision for a nonprobate transfer of community property on the death of a married person, regardless of whether the provision

for transfer of the property was executed by the person, or written consent to the provision for transfer of the property was given by the person's spouse, before, on, or after January 1, 1993.

(b) Subdivision (c) of Section 5030 does not apply, and the applicable law in effect on the date of death does apply, to revocation of a written consent given by a spouse who died before January 1, 1993.

Comment. Section 5014 is an exception to the rule stated in Section 3 (general transitional provision). To the extent this chapter changes the law governing the rights of successors of a person who gives written consent to a nonprobate transfer by the person's spouse, this chapter does not seek to apply the change in law to rights that vested as a result of a death that occurred before the operative date of the chapter.

Article 2. Consent to Nonprobate Transfer

§ 5020. Written consent required

5020. A provision for a nonprobate transfer of community property on death executed by a married person without the written consent of the person's spouse (1) is not effective as to the nonconsenting spouse's interest in the property and (2) does not affect the nonconsenting spouse's disposition on death of the nonconsenting spouse's interest in the community property by will, intestate succession, or nonprobate transfer.

Comment. Section 5020 is comparable to Civil Code Section 5125(b). It codifies the case law rule that the statutory community property gift limitations apply to nonprobate transfers such as beneficiary designations in trusts and accounts. See, e.g., Tyre v. Aetna Life Insurance Co., 54 Cal. 2d 399, 353 P. 2d 725, 6 Cal. Rptr. 13 (1960) (beneficiary designation in bank trust account); Yiatchos v. Yiatchos, 376 U.S. 306 (1964) (beneficiary designation for United States Savings Bonds).

It should be noted that while Section 5020 makes clear that a nonconsenting spouse retains full dispositional rights over the spouse's community property interest (subject to overriding governing principles as provided in Section 5011), this does not imply that a consenting spouse loses these rights. A written consent is revocable during the spouse's lifetime, and a revocation and contrary disposition may be made by will. See Section 5031 (form and delivery of revocation).

Section 5020 does not affect the principle that a holder of property may transfer the property as specified in the instrument. Section 5003 (protection of holder of property). But the actions of the holder do not affect rights between the spouses and their successors. See Section 5012 (community property rights independent of transfer obligation).

§ 5021. Transfer without written consent

5021. (a) In a proceeding to set aside a nonprobate transfer of community property on death made pursuant to a provision for transfer of the property executed by a married person without the written consent of the person's spouse, the court shall set aside the transfer as to the nonconsenting spouse's interest in the property, subject to the terms and conditions or other remedy that appears equitable under the circumstances of the case, taking into account the rights of all interested persons.

(b) Nothing in ~~this section~~ subdivision (a) affects any additional remedy the nonconsenting spouse may have against the person's estate for a nonprobate transfer of community property on death without the spouse's written consent.

Comment. Subdivision (a) of Section 5021 is consistent with the rule applicable to present gifts of community property at termination of the marriage by dissolution or death. See, e.g., Ballinger v. Ballinger, 9 Cal. 2d 330, 70 P. 2d 629 (1937); Gantner v. Johnson, 274 Cal. App. 2d 869, 79 Cal. Rptr. 381 (1969). It implements the concept that a nonprobate transfer is a will substitute, and that a person has the right to direct a transfer of the person's one-half interest in the community property at death, with or without the spouse's consent. See, e.g., Sections 100-102 (effect of death of married person on community and quasi-community property), 6101 (property which may be disposed of by will).

Under subdivision (a) the court has discretion to fashion an appropriate order, depending on the circumstances of the case. The order may, for example, provide for recovery of the value of the property rather than the particular item, or aggregate property received by a beneficiary instead of imposing a division by item.

Subdivision (b) makes clear that this section does not provide the exclusive remedy where a person has directed a nonprobate transfer of community property without the written consent of the other spouse. It may be proper, for example and without limitation, simply to allow the surviving spouse, instead of or in addition to proceeding against the beneficiary of the nonprobate asset, to proceed against the decedent's estate for an offset for the value of the property transferred out of the share of the decedent, or to give the surviving spouse a right of reimbursement.

Staff Note. The changes shown in strikeout and underscore are suggested by State Bar Team 2. They are consistent with our intent in this section, and the staff would make these changes.

Order of Priority

Team 2 would also go further and specify an order of priority--the nonconsenting spouse should proceed first against the beneficiary of the nonprobate transfer and, if not recoverable, then against other community assets. The staff opposes such a rigid formula; this is

presumptively the way it should be done, but as Team 2 suggests, "the Court is in the best position to take into account the rights of all interested parties."

Item v. Aggregate Theory

This is emphasized in the letter from Gregory Wilcox, who invokes the old troublesome problem of the item versus aggregate theory of community property. The item theory argues that each spouse has a one-half interest in each individual item of community property; the aggregate theory contends that each spouse has a one-half interest in the community property as a whole, and not in any particular item. Thus if a deceased spouse by will disposes of a particular item of community property, the item theory would limit the disposition to one-half that item, whereas the aggregate theory would allow disposition of the whole item, so long as it is offset by other community property of equal value going to the surviving spouse.

California adheres to the item theory, and for good reason. The aggregate theory would allow the first deceased spouse to pick and choose which assets to dispose of, leaving the surviving spouse with rejected items. Moreover, the aggregate theory would be difficult to administer, since it would require valuation of community property to ensure that not more than an aggregate of 50% of the community property had been disposed of; and where more than 50% had been disposed of, it would require difficult abatement decisions. The item theory avoids all these problems, but enables the surviving spouse to make a sensible election between the decedent's purported disposition and a claim for 50% of each item.

However, the logic of the item theory tends to break down when we get to fungible property (including cash). If the community has 20 identical shares of stock, shouldn't the decedent's will of 10 shares be honored, since each spouse in effect owns a net 10 shares? If we say the will is good only as to one-half of each of the 10 shares disposed of, this leaves the remaining one-half of each of the 10 shares to the survivor, plus all of the undisposed of 10 shares; in other words, the surviving spouse would end up with the equivalent of 15 shares of stock and the beneficiary, only 5. Not to mention the problem of having to partition the tenancy in common ownership of the 10 shares between the surviving spouse and the beneficiary.

Mr. Wilcox points out that these problems are compounded in the context of a nonprobate transfer. Assume a community estate of $20,000 cash. The decedent's will presumably could give legacies amounting to $10,000 without the consent of the surviving spouse. But if the decedent, instead of giving legacies, were to create Totten trusts amounting to $10,000 for the beneficiaries without the consent of the surviving spouse, each Totten trust would be good only as to one-half. This is the holding (or at least dictum) in Estate of Wilson, 183 Cal. App. 3d 67, 277 Cal. Rptr. 794 (1986), which states that "while the decedent cannot leave a third party the entire balance of an account which has $10,000 of community property in it and is held as trustee for the third party, the decedent can, by will, leave a legacy of $10,000 to the third party from his one-half share of the community property."

Despite these problems, the item theory nonetheless remains the only workable approach to a nonprobate transfer of community property. There is no way of knowing whether any particular nonprobate transfer, either alone or with other nonprobate transfers, is more than 50% of

the community estate, particularly since there is no probate proceeding to collect and value all assets. In a will, the decedent may effectively dispose of the decedent's entire one-half aggregate interest in community property through a residuary clause. But a nonprobate transfer necessarily disposes of specific items of property.

Section 5021 does address the item versus aggregate problem. As Mr. Wilcox notes, this section provides that a nonprobate transfer of community property without the consent of a spouse must be set aside as to the nonconsenting spouse's interest "subject to the terms and conditions or other remedy that appears equitable under the circumstances of the case." The Comment notes that the court has discretion to fashion an appropriate order. "The order may, for example, provide for recovery of the value of the property rather than the particular item, or aggregate property received by a beneficiary instead of imposing a division by item." The staff believes this is the best we can do in this particularly thorny area, and would not address the matter further.

Unilateral Encumbrances

On a related matter, Frieda Gordon Daugherty of the Women Lawyers' Association of Los Angeles, Family Law Section, notes that State Bar Conference of Delegates has adopted a resolution to overrule another Supreme Court case, Droeger v. Friedman, Sloan & Ross, which holds that a married person cannot unilaterally encumber community real property without the consent of the person's spouse. This case follows a former Law Revision Commission recommendation. According to Ms. Daugherty, the State Bar resolution would permit a married person to encumber or transfer a one-half interest in community property without spousal consent, provided notice is given to the spouse within a specified period of time.

Ms. Daugherty notes that this proposal is conceptually related to the present recommendation on nonprobate transfers, which also validates a transfer of a one-half interest in community property without spousal consent. However, the encumbrance proposal would go much farther by validating lifetime transfers, unlike the present recommendation which only validates unconsented to transfers at death, consistent with traditional community property principles.

Ms. Daugherty would like to coordinate the two pieces of legislation in some way. The staff would like to hear specific proposals on this, but would be wary of tying the two pieces of legislation together, since the State Bar proposal makes a substantial departure from traditional community property protections for married persons.

§ 5022. Written consent not a transmutation

5022. (a) Except as provided in subdivision (b), a spouse's written consent to a provision for a nonprobate transfer of community property on death is not a transmutation of the consenting spouse's interest in the property.

(b) This chapter does not apply to a spouse's written consent to a provision for a nonprobate transfer of community property on death that

satisfies Section 5110.730 of the Civil Code. Such a consent is a transmutation and is governed by the law applicable to transmutations.

Comment. Section 5022 is consistent with the result in Estate of MacDonald, 51 Cal. 3d 262, 794 P.2d 911, 272 Cal. Rptr. 153 (1990). A consent to a nonprobate transfer is in effect a consent to a future gift of the person's interest in community property, and is subject to the legal incidents provided in this chapter. Until the gift is complete, however, it remains community property and is part of the community estate for purposes of division of property at dissolution of marriage until the consent becomes irrevocable by the death of either spouse. See Section 5030 (revocability of written consent). However, if the consent specifies a clear intent to transmute the property, the expression of intent controls over this section. See Section 5011(c) (governing provision of consent).

Staff Note. We have revised the Comment in response to a suggestion by Mr. Wilson.

§ 5023. Effect of modification

5023. (a) As used in this section "modification" means revocation of a provision for a nonprobate transfer on death in whole or part, designation of a different beneficiary, or election of a different benefit or payment option.

(b) If a married person executes a provision for a nonprobate transfer of community property on death with the written consent of the person's spouse and thereafter executes a modification of the provision for transfer of the property without written consent of the spouse, the modification is effective as to the person's interest in the community property and has the following effect on the spouse's interest in the community property:

(1) If the person executes the modification during the spouse's lifetime, the modification revokes the spouse's previous written consent to the provision for transfer of the property.

(2) If the person executes the modification after the spouse's death, the modification does not affect the spouse's previous written consent to the provision for transfer of the property, and the spouse's interest in the community property is subject to the nonprobate transfer on death as consented to by the spouse.

(3) If a written expression of intent of a party in the provision for transfer of the property or in the written consent to the provision for transfer of the property authorizes the person to execute a modification after the spouse's death, the spouse's interest in the

community property is deemed transferred to the married person on the spouse's death, and the modification is effective as to both the person's and the spouse's interests in the community property.

Comment. Section 5023 treats a modification of a nonprobate transfer during the lifetimes of the spouses as a new nonprobate transfer, as to which the living spouse may consent if so desired. If the spouse does not have legal capacity to consent at the time, consent may be obtained through substituted judgment procedures. See Section 2580 (substituted judgment). Failure of consent to the changed terms revokes the original consent to the nonprobate transfer, and the spouse's interest passes with the spouse's estate or as otherwise disposed of by the spouse. See Section 5032 (effect of revocation). It should be noted that a modification is subject to the right of the decedent to make a contrary disposition by will. Section 5031 (form and delivery of revocation).

A modification by the surviving spouse after the death of the other spouse does not affect the nonprobate transfer of the community property interest of the deceased spouse as consented to by the deceased spouse. In effect, the consent is itself a nonprobate transfer which becomes irrevocable on the death of the spouse. See Section 5030 (revocability of consent). The deceased spouse's interest in the community property is transferred as consented to by the deceased spouse, unless by the terms of the consent the deceased spouse has authorized the surviving spouse to make modifications in the nonprobate transfer. This is a special instance of the rule stated in Section 5011 that a nonprobate transfer of community property on death is governed by overriding principles, including a written expression of intent.

Note. The Commission particularly solicited comment on this section.

The Beverly Hills bar group supports this section, Team 2 of the State Bar strongly supports the section, and the Executive Committee has also voted unanimously in support. The one concern of Team 2 is that subdivision (b)(3) invites the spouses to agree to what is in effect a general power of appointment, possibly triggering a significant economic shift and severe tax consequences. Some members of Team 2 felt that any forms developed under subdivision (b)(3) might incorporate warning language suggesting that the parties seek legal or tax advice before executing what is in effect a general power of appointment. The staff believes that this would be worthwhile, but notes that the Commission has considered the possibility of providing statutory form language on this point on two different occasions in the past and both times has rejected the concept.

Melvin Wilson of Security Pacific Bank also approves this section, although his comments seem to be based on an earlier draft, or to indicate a misunderstanding of the Commission's proposal. Under the tentative recommendation, the surviving spouse would have full power to deal with and dispose of the both halves of the community property only if the parties specifically give the surviving spouse that authority. But Mr. Wilson's approving comments appear to support the "Halbach approach" that would automatically give the surviving spouse full dominion over the community property. He argues that it is appropriate for the surviving spouse to have the unrestricted right to modify the plan after the death of a consenting spouse "because that seems

consistent with the inferred intent of the spouses. When a consenting spouse consents to a dispositive plan which bypasses him or her, it is reasonable to infer that he or she understands and approves both the plan and the consequences of the consent. It is also reasonable to infer that the consenting spouse intends such waiver to become effective on his or her prior death and that the effect of such waiver is to confer on the surviving depositor spouse all of the incidents of ownership over the affected property."

Article 3. Revocation of Consent

§ 5030. Revocability of written consent

5030. (a) A spouse's written consent to a provision for a nonprobate transfer of community property on death is revocable during the marriage.

(b) On termination of the marriage by dissolution, the written consent is revocable and the community property is subject to division under Section 4800 of the Civil Code or other disposition on order within the jurisdiction of the court.

(c) On the death of either spouse, the written consent is irrevocable.

Comment. Section 5030 is subject to express terms to the contrary. See Section 5011 (governing provision of instrument, law, or consent). If the consent is part of a mutual estate plan, nothing in this section precludes enforcement of the mutual estate plan by appropriate remedies, including an injunction affecting revocation.

Subdivision (c), to the extent it relates to the death of the consenting spouse, overrules the effect of Estate of MacDonald, 51 Cal. 3d 262, 794 P.2d 911, 272 Cal. Rptr. 153 (1990). The consent of a spouse to disposition of the spouse's one-half interest in the community property is subject to a contrary disposition in the spouse's will. Section 5031. The spouse's personal representative may not revoke the consent to a nonprobate transfer and impose a different estate plan on the spouse's property.

The surviving spouse may modify a provision for a nonprobate transfer of community property previously consented to by the deceased spouse to the extent provided in Section 5023.

It should be noted that these changes in the law are subject to Section 5014 (transitional provision).

Staff Note. Team 2 would split up subdivision (c) to deal with the death of the donor spouse and the death of the consenting spouse separately, thus:

> *(c) On death of the transferor spouse, the written consent is irrevocable.*
>
> *(d) On death of the consenting spouse, the written consent is governed by §5023 above.*

The staff is opposed to this change for several reasons. First, it destroys the conceptual unity that termination of marriage by death terminates the opportunity to revoke the consent. Second, it mixes the concept of revocability of consent with the concept of modification of terms. In fact, on death of the consenting spouse the revocability of consent is not governed by Section 5023, and the consenting spouse's share cannot be recalled to the estate; Section 5023 deals with alternate dispositions of the consenting spouse's share after the consenting spouse's death, not with the ability of the consenting spouse's successors to revoke the consent. Third, it would require more complex drafting to split subdivision (c), since more precise references to the roles of the different spouses would be required--"transferor spouse" has no antecedent, is not used elsewhere in the draft, and is ambiguous where both spouses have joined in the transfer.

Team 2 also suggests Comment revisions. The staff has incorporated the substance of one of their suggested revisions, as marked above. The Team also would note that to the extent the statute precludes revocation on death of the donor spouse, it continues existing law. The staff would not say this, since we do not believe there is any law on this point.

Frieda Gordon Daugherty of the Women Lawyers' Association of Los Angeles, Family Law Section, would address the issue of the effectiveness of a designation of beneficiaries where death occurs during the pendency of a dissolution proceeding. The Commission has on a number of occasions in the past considered whether the filing of a dissolution proceeding should have the effect of revoking a will or altering beneficiary designations, and has always come to the conclusion that it should not. Many dissolution proceedings are filed and thereafter abandoned when the parties reconcile. In addition, many times the parties want to have their beneficiaries remain the same and would not want their estate plans destroyed by operation of law. The lawyers for the parties to a dissolution proceeding should have their clients review their particular circumstances and revoke or not their beneficiary designations as may be appropriate; self-help manuals should advise the same.

§ 5031. Form and delivery of revocation

5031. (a) If a married person executes a provision for a nonprobate transfer of community property on death with the written consent of the person's spouse, the consenting spouse may revoke the consent by a writing, including a will, that identifies the provision for transfer of the property being revoked, and that is delivered to the married person before the married person's death.

(b) Revocation of a spouse's written consent to a provision for a nonprobate transfer of community property on death does not affect the authority of the holder of the property to transfer the property in compliance with the provision for transfer of the property to the extent provided in Section 5003.

Comment. Section 5031 is consistent with subdivision (c) of Section 5030 (written consent irrevocable on death). Under this section any specific and delivered writing is sufficient, including a document purporting to be a will, whether or not admitted to probate. The will provision would change existing law as to life insurance by allowing the beneficiary designation to be overridden by an express provision in a will.

This section is subject to a contrary provision in the instrument, and the instrument may include terms that specify the manner of revocation of consent. Section 5011 (governing provision of instrument, law, or consent).

It should be noted that a consent is irrevocable, regardless of the observance of the formalities of this section, on the death of either spouse. See Section 5030 & Comment (revocability of written consent).

Staff Note. State Bar Team 2 believes the delivery requirement for revocation of consent should be revised so that the revocation is only effective if delivered under circumstances that allow the donor a reasonable opportunity to make corresponding changes in the estate plan necessitated by the revocation of consent. The Team recognizes that the "reasonable opportunity" approach may generate litigation; nonetheless, the delivery requirement should be converted from a "mechanical concept to one based upon fundamental fairness."

The staff does not believe it is good policy to make the effectiveness of withdrawn consent depend on the circumstances of the other spouse. Each spouse should have maximum control over that spouse's share of the community property, including the right to withdraw consent and change the disposition of that spouse's interest in the property during the marriage. The requirement of delivery before death serves the dual function of avoiding secret changes and enabling the other spouse to take responsive action. But this should not be carried to the extreme that it denies a spouse the reasonable right to control the spouse's interest in community property.

The Beverly Hills Bar group wants to make sure that a spouse's personal representative may not revoke the spouse's consent after the spouse's death, as was done in MacDonald. This is the effect of the recommendation, since the preceding section makes consent irrevocable on death of either spouse. We have added language to the Comment to this section to make this interrelation clear.

§ 5032. Effect of revocation

5032. On revocation of a spouse's written consent to a nonprobate transfer of community property on death, the property passes in the same manner as if the consent had not been given.

Comment. Section 5032 governs the substantive rights of the spouses in the community property notwithstanding overriding contractual and legal requirements that bind a holder of the community property. See Sections 5003 (protection of holder of property), 5012 (community property rights independent of transfer obligation). However, this section is subject to contrary terms of the instrument and to overriding law governing the obligation of a holder of community

property to deal with the property under the particular type of instrument. See Section 5011 (governing provision of instrument, law, or consent).

For rights of a spouse who has not given written consent, see Section 5020 (written consent required).

CONFORMING CHANGES

Civ. Code § 5110.740 (amended). Estate planning documents

SEC. . Section 5110.740 of the Civil Code is amended to read:

5110.740. (a) A statement in a will of the character of property is not admissible as evidence of a transmutation of the property in any proceeding commenced before the death of the person who made the will.

(b) A waiver of a right to a joint and survivor annuity or survivor's benefits under the federal Retirement Equity Act of 1984 is not a transmutation of the community property rights of the person executing the waiver.

(c) A written joinder or written consent to a nonprobate transfer of community property on death is a transmutation and is governed by the law applicable to transmutations and not by Chapter 2 (commencing with Section 5010) of Part 1 of Division 5 of the Probate Code) if the written joinder or written consent satisfies Section 5110.730.

Comment. Under subdivision (b) of Section 5110.740, a waiver for federal tax purposes is not a transmutation within the meaning of Section 5110.710.

Subdivision (c) is consistent with Probate Code Section 5022 (written consent not a transmutation).

Prob. Code § 141 (amended). Rights that may be waived

SEC. . Section 141 of the Probate Code is amended to read:

141. (a) The right of a surviving spouse to any of the following may be waived in whole or in part by a waiver under this chapter:

...

(10) An interest in property that is the subject of a nonprobate transfer on death under Part 1 (commencing with Section 5000) of Division 5.

(b) Nothing in this chapter affects or limits the waiver or manner of waiver of rights other than those referred to in subdivision (a), including but not limited to the right to property that would pass from the decedent to the surviving spouse by nonprobate transfer upon the death of the decedent such as the survivorship interest under a joint tenancy, a Totten trust account, or a pay-on-death account.

Comment. Paragraph (10) is added to Section 141(a) for purposes of cross-referencing the provisions on nonprobate transfers. See also Section 5013 (waiver of rights in community property). Paragraph (10) is a specific instance of the general rule stated in subdivision (b).