#F-521.1/L-521.1

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03/11/92

First Supplement to Memorandum 92-17

Subject: Study F-521.1/L-521.1 - Community Property in Joint Tenancy Form (Comments on Consultant's Background Study)

Memorandum 92-17 includes comments received on Professor Kasner's background study on community property in joint tenancy form. Attached to this supplement are additional comments from Professor June Miller Weisberger of University of Wisconsin Law School (Exhibit 1), Professor William A. Reppy of Duke Law School and a Commission consultant on community property law (Exhibit 2), and Ronald C. Pearson of Los Angeles on behalf of the Executive Committee of the Probate and Trust Law Section of the Los Angeles County Bar Association (Exhibit 3). Their comments are analyzed below.

Community Property with Right of Survivorship

Wisconsin's Marital Property Act, operative in 1986, adopts a community property type regime for Wisconsin marital property. The law adopts a new form of tenure--"survivorship marital property"--which has community property attributes but passes by right of survivorship at death. Any marital property titled as joint tenancy is statutorily recognized as survivorship marital property.

Professor Weisberger (Exhibit 1) indicates that Wisconsin practitioners have been assured that Wisconsin's survivorship marital property "will be treated by IRS as a form of community property for the determination of income tax capital gains basis when the first spouse dies and the property is subsequently sold by the surviving spouse."

The Los Angeles County group (Exhibit 3) does not believe a new title form would be helpful in California. It would "confuse even further exactly those persons whom the law seeks to help -- married couples taking title in joint tenancy and their advisors. Introduction of a separate written interspousal agreement to implement this new form

of title, as in Texas or Wisconsin, would be unworkable due to its complexity. People would be ignorant of the requirement, or they would ignore it."

Expansion of Civil Code § 4800.1

Professor Kasner's main recommendation is that spousal joint tenancies be treated as community property for all purposes, not just dissolution, except that a right of survivorship should be imposed on the property. The Los Angeles County group (Exhibit 3) proposes a variation on this approach. Their proposal has the following features:

(1) Marital joint tenancy property would be presumed community property for all purposes.

(2) The right of survivorship inherent in joint tenancy would be recognized as a testamentary disposition of the community property to the surviving spouse.

(3) Termination or transfer of an interest in the property requires notice to the other spouse.

(4) Tracing of separate property contributions would be permitted.

(5) Creditors would have the same rights as in community property.

(6) The community property presumption would be rebuttable by showing a transmutation to separate property.

(7) The new rules would apply to estates of decedents who die after the operative date of the new act.

Transmutation Issues

Professor Reppy (Exhibit 2) comments on the interrelation of the transmutation statute with the community property presumption at dissolution of marriage. Professor Reppy agrees with Professor Goda that the transmutation statute overrides the community property presumption. They disagree with Professor Kasner and the staff that the community property presumption overrides the transmutation statute. Professor Reppy points out that this "should suggest to you a statutory amendment is appropriate to avoid a lot of litigation to settle the dispute between us."

At issue here is the property rights of spouses at dissolution of marriage. Assume the spouses acquire property during marriage in joint tenancy form. At dissolution of marriage, is it divided equally between the spouses, or do we look to the source of the acquisition funds as community or separate to determine the property rights of the spouses?

There are a number of important statutes that bear on this issue, cited in the materials provided by Professors Kasner, Goda, and Reppy. All these enactments are the result of Law Revision Commission recommendations.

The transmutation statute, Civil Code Section 5110.730, was enacted in response to California's "easy transmutation" system. A transmutation is a conversion of ownership rights in property, typically from separate property of a spouse to community property of both spouses, or from community property of both spouses to separate property of one spouse. To correct abuses of California's easy transmutation system, Section 5110.730 provides that:

> A transmutation of real or personal property is not valid unless made in writing by an express declaration that is made, joined in, consented to, or accepted by the spouse whose interest in the property is adversely affected.

The property division statutes, Civil Code Sections 4800.1 and 4800.2, were enacted in response to Marriage of Lucas, 27 Cal. 3d 808 (1980). In that case property was acquired in joint tenancy form using the separate property of one spouse. When the marriage was dissolved six months later, the court awarded half the property to each spouse on a theory of gift inherent in the title form. Sections 4800.1 and 4800.2 address this inequity by providing that at dissolution of marriage property in joint tenancy form is presumed to be community, but separate property contributions to its acquisition are first reimbursed before dividing the community. Under Section 4800.1, the presumption that property in joint tenancy form will be considered community for purposes of division at dissolution is rebuttable:

> This presumption is a presumption affecting the burden of proof and may be rebutted by either of the following:
>
> (1) A clear statement in the deed or other documentary evidence of title by which the property is acquired that the property is separate property and not community property.
>
> (2) Proof that the parties have made a written agreement that the property is separate property.

The reimbursement right for separate property contributions applies under Section 4800.2 unless a party has made a written waiver of the right to reimbursement.

Getting back to our original issue, how do we divide property acquired during marriage in joint tenancy form--equal division, or division based on source of funds?

Suppose the property was taken in joint tenancy form using community funds. Under Section 4800.1 this is presumed community notwithstanding the form of title, there is no evidence to rebut the presumption, and the property should be divided equally as community property. Does the transmutation statute, Section 5110.730, affect this analysis? If the taking of title as joint tenancy is a transmutation of the community property to the separate property of both spouses, ownership would be in equal shares and the court would have jurisdiction to divide the property under Section 4800.4. The result is the same in either case--equal division between the spouses.

Suppose the property was taken in joint tenancy form using separate funds of one spouse. This is the Lucas case, and application of Sections 4800.1 and 4800.2 would reimburse the separate contributions and divide any surplus equally. If Section 5110.730 (the transmutation statute) is applied to this property, the results could differ dramatically. If the joint tenancy title amounts to a transmutation of separate property of one spouse to separate property of both spouses, there would be a gift of one half. If the joint tenancy title does not amount to a transmutation, the property should be confirmed to the acquiring spouse at dissolution.

Which statutes, then, do we apply to a division of spousal property held in joint tenancy form--the transmutation statute, the property division statute, or both? Professor Kasner and the staff have argued that you apply only the property division statute--this is a special statute designed to cover rights at dissolution of marriage, and governs regardless of the general rules governing transmutations for other purposes. Professors Goda and Reppy argue that you must read the two statutes together, although they seem to vary in just how this would be done. Also involved is the issue of whether acquisition of property in joint tenancy form, without more, is or should be a transmutation under Section 5110.370, as interpreted by the courts.

The staff agrees with all the professors that there is enough uncertainty here to warrant clarification. At this point the staff thinks we need more input on this issue from other interested persons, including both the family law bar and the estate planning bar, before we make policy decisions on it.

Respectfully submitted,

Nathaniel Sterling
Executive Secretary

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February 21, 1992

Memo to: Professor Jerry A. Kasner

From: Professor June M. Weisberger

Re: Background Study Concerning Community Property in Joint Tenancy Form.

I received in today's mail a copy of your background study for the California Law Revision Commission.

Since your discussion does not include Wisconsin expressly, I am including several pages from a 1985 article which I wrote on Wisconsin's Marital Property Act, a modified version of the Uniform Marital property Act. (Wisconsin became a community property state on 1/1/86. Wisconsin's "basic" community property law may be found in Chapter 766 of the Wisconsin Statutes.)

Wisconsin practitioners have been assured that Wisconsin's "survivorship marital property" will be treated by IRS as a form of community property for the determination of income tax capital gains basis when the first spouse dies and the property is subsequently sold by the surviving spouse.

By separate cover, I am sending to you a full copy of the 1985 article and a more recent article appearing in 1990 Wisconsin Law Review. You may be particularly interested in another IRS and community property issue discussed in the latter article (pp. 790-793).

Please do not hesitate to call me if you have any questions about Wisconsin's community property legislation and how it has been working during the past six years.

EXHIBIT 2

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March 3, 1992

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RE: Memorandum 92-17

Dear Nat:

Your memo came to me a day after I had revised my Gilbert's summary on California Community Property law to deal with whether acceptance of a deed reciting joint tenancy (or any other form of co-ownership) can work a transmutation to the recited form of ownership when funds used to pay for the asset were of a different character. At divorce whether there has been a community to joint tenancy transmutation is, on one issue, irrelevant because section 4800.4 allows dividing joint tenancy as if it were community.

At divorce section 4800.1's presumption of community property based on a recital of any form of co-ownership is important (a) if it triggers the right of reimbursement for separate contributions created in section 4800.2 and (b) if separate funds were used for all or part of the acquisition the presumption supplants the need for an express writing under section 5110.730 to transmute the separate funds to co-owned property. The deed just won't contain the express language *MacDonald* requires. Before section 5110.730 took effect, Marriage of Benart, 160 Cal. App. 3d 183 (1984), did hold that taking joint ownership title did cause a transmutation of separate funds.

On point (a), it may be that the word "form" in section 4800.1 means that a transmutation is worked by section 4800.1 itself even though it would be unsuccessful under other rules of law. If so, 4800.2 undoes the gift to the extent of allowing reimbursement. On both points (a) and (b) you and Kasner think enactment of section 5110.730 had no effect on decisions like *Benart*. Your own view I understand to be that section 4800.1 is the specific statute (applicable only at divorce) and it prevails over the broader section 5110.730.

I agree with Msgr. Goda that this is not correct. Notwithstanding use of the word "form," section 4800.1 has always not come into play until a successful transmutation to joint tenancy (or to other form of co-ownership) was established. Its very purpose was to undo that transmutation. It does not assist parties in making transmutations but denies the effect of a transmutation already made. Section 5110.730 is the only statute telling one **how** to effectuate a transmutation.

Thus, where H takes his separate money and buys land with a joint tenancy title, his acceptance of the deed does not work a transmutation because the deed lacks the recital required by *MacDonald* that monies other than joint tenancy funds were used for the purchase. The deed will not show H is giving up anything, and *MacDonald* bars all extrinsic evidence. The property is H's separate property despite the recital even at divorce. At death there is no right of survivorship; during the marriage there is no interest reachable by W's nonnecessaries creditors. At divorce there is no joint ownership for section 4800.1 to presume is community ownership (to trigger applicability of the reimbursement rights under section 4800.2).

At the very least, Nat, the fact two intelligent law professors (Goda and I -- no need for modesty here) believe in the correctness of the above analysis should suggest to you a statutory amendment is appropriate to avoid a lot of litigation to settle the dispute between us. The way to do it is to abrogate *MacDonald* by amending section 5110.730 to provide that recitals in deeds accepted by spouses are sufficient writing to transmute to the form of title so recited.

I was interested in the point made on page 2 of your memo that the IRS has changed course and now denies a stepped up basis if joint tenancy is recited even though the attempted transmutation failed. This is cause for enactment of a law providing some simple way for spouses to reform joint tenancy deeds to eliminate such a recital so the very useful stepped up basis for survivor's half interest is available. Does the IRS position mean that Nevada's "community property with right of survivorship" (which is not joint tenancy for management and creditors' rights purposes) loses the stepped up basis? I have missed the publication giving the new IRS position. Can you supply me a cite or a copy of what you are referring to at page 2 of the memo? Thanks.

Sincerely,

Bill

William A. Reppy, Jr.
Professor of Law

WAR:jma

CC: Paul J. Goda

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March 10, 1992

VIA FAX

Mr. Nathaniel Sterling
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Re: Study F-521.1/L-521.1
Community Property in Joint Tenancy Form.

Dear Mr. Sterling:

The Executive Committee of the Probate and Trust Law Section of the Los Angeles County Bar Association has reviewed Professor Kasner's report entitled "Community Property in Joint Tenancy Form: Since We Have It, Let's Recognize It." Although complete unanimity was not achieved, the comments set forth below reflect the views of the majority of the Committee.

1. Use of Joint Tenancy by California Spouses.

The Committee agrees with Professor Kasner's statement that the majority of married couples in California take title to property as joint tenants in order to avoid probate administration of the asset. As the study points out, the average couple buying a home or opening a brokerage account has little or no understanding of the legal or tax consequences of joint tenancy title.

Although the strict requirements for transmutation of community to separate property contained in Civil Code Section 5110.730 and the MacDonald case create substantial doubt as to the current status of joint tenancies created after 1985 by married couples, this lack of clarity in the law may be seen as benefiting spouses, since failure to satisfy statutory dictates should result in their property being treated as community. Nevertheless, we believe that the status of spousal joint tenancy property at death should be clarified and synchronized with the status of spousal joint tenancy property upon dissolution of marriage.

2. New Form of Title - "Community Property with Right of Survivorship."

Although the Committee recognizes the need for clarification of the status of spousal property held under joint tenancy title in California, we do not believe that creation of a new form of title is required at this time. We fear that introduction of "survivorship marital property" or "community property with the right of survivorship" as a new titleholding vehicle will confuse even further exactly those persons whom the law seeks to help -- married couples taking title in joint tenancy and their advisors.

Introduction of a separate written interspousal agreement to implement this new form of title, as in Texas or Wisconsin, would be unworkable due to its complexity. People would be ignorant of the requirement, or they would ignore it.

A new statutory form of title, such as found in the Uniform Act, might be more successful. However, substantial education of the public and various professionals would be necessary to ensure that "community property with right of survivorship" is properly understood and utilized. We do not believe that resources are available at this time for such education. Therefore, we suspect that most couples would continue to take title in joint tenancy, defeating the goal of the proposed legislation.

2. Presumption of Community Property.

The Executive Committee recommends that the status of spousal joint tenancy property be clarified by the inclusion in the Probate Code of a presumption that property held in joint tenancy title by married persons is community property for all purposes, except that the right of survivorship shall be recognized as a testamentary disposition of the deceased spouse's interest in the property to the surviving spouse. One spouse may not terminate the joint tenancy or transfer his or her interest without notice to the other. Tracing of separate property contributions is permitted in accordance with California case law. Creditors are protected by access to the property during lifetime and after death. Furthermore, the IRS should accept the community property nature of such property.

This statutory presumption shall affect the burden of proof and may be rebutted by evidence sufficient to satisfy Civil Code Section 5110.730. However, we suggest that merely executing escrow instructions which show title to be vested as "joint

tenants with rights of survivorship" should not suffice to rebut the statutory presumption of community property.

The statutory presumption shall be applicable to estates of decedents, who die after the effective date of the legislation. This ensures predictability and a smooth transition, permitting couples who wish to hold property in true joint tenancy to execute a written agreement, memorializing the transmutation of their community property to joint tenancy.

4. Conclusion.

The Executive Committee hopes that lenders, title companies, trust companies and consumers will present their views on this wide reaching proposed change in the law.

Our recommendation discussed above is a variation upon the theme developed by Professor Kasner in his study. Our suggestion is clearly only a broad stroke sketch, requiring intricate detail work before it can become a workable alternative.

We appreciate the opportunity to present our thoughts and look forward to following this study with great interest.

Very truly yours,

Ronald C. Pearson

RONALD C. PEARSON

RCP:ms
cc: Executive Committee