Study FHL-910 May 15, 1998

Memorandum 98-35

Effect of Dissolution of Marriage on Nonprobate Transfers: Comments on Tentative Recommendation

BACKGROUND

In January 1997, the Commission circulated a tentative recommendation proposing that dissolution or annulment of marriage (hereinafter "divorce") sever a joint tenancy as between the former spouses. This proposal was intended to implement the likely intentions of those who fail to sever a marital joint tenancy after a divorce. The public response to that proposal was generally positive. Some commentators suggested that the scope of the proposed law should be expanded so that divorce would revoke all nonprobate transfers to a former spouse and not just joint tenancy. This would broaden the beneficial effect of the proposal and lead to greater consistency in the law governing transfers on death. The Commission agreed and developed a tentative recommendation to that effect.

This memorandum reviews comments we have received regarding the second tentative recommendation (Tentative Recommendation relating to the Effect of Dissolution of Marriage on Nonprobate Transfers (January 1998)). Comment letters are attached in the Exhibit as follows:

GENERAL REACTION

Response to the tentative recommendation was mixed. Ms. Ratzlaff "wholeheartedly" supports the proposal. In her experience, many people erroneously assume that divorce revokes nonprobate transfers automatically. She

also points out that some forms of nonprobate transfer are not readily apparent or are easily forgotten (e.g., a life insurance policy that is an automatic component of a credit union account). Even a person who understands existing law and takes steps to revoke all nonprobate transfers to a former spouse might overlook such instruments. See Exhibit p. 4.

The Executive Committee of the State Bar Estate Planning, Trust and Probate Law Section (Executive Committee) supports the proposed law, believing it will implement the likely intention of divorcing parties. However, the Executive Committee believes that the transitional provision should be changed to account for the incapacity of a transferor during the transitional "grace period." See Exhibit pp. 9-10. This is discussed below.

The California Land Title Association (CLTA) believes that the proposed law's purpose is "laudable," but has serious concerns about its practical effect, in particular, its effect on those who remain married.

> The practical consequence of the proposed law is to unfairly shift responsibility for protecting certain members of society: **from** those who are actively involved in a dissolution and who should be responsible (with their legal counsel) to effect revocation of such nonprobate transfers as a part of their dissolution **to** those who are married hoping to effect their last wishes through proper estate planning with the expectation that such planning will reduce or eliminate unnecessary burdens on their surviving spouse.

See Exhibit p. 8 (emphasis in original). CLTA does not support the proposed law in its present form. CLTA's concerns and suggestions are discussed below.

Mr. Fulton generally objects to the proposal as being overly paternalistic. "The law cannot protect us from everything." See Exhibit p. 1. He also questions the basis for the "clear and convincing evidence" standard employed in an exception to the proposed law. See Exhibit p. 2. This question is discussed below.

Mr. Sutton opposes the proposal. He believes it will inappropriately undermine the certainty of joint tenancy title. "If a divorcing person leaves a former spouse as the surviving joint tenant on real property, so be it. He/she should have hired an attorney." See Exhibit p. 3.

NOTICE FORM ALTERNATIVE

CLTA opposes the proposed law in its present form. It suggests, as a complete alternative, the creation of a separate notice form to be used in a divorce

proceeding, warning the parties of the need to make changes to nonprobate transfers or joint tenancy title to reflect their post-divorce intentions. This form would be executed by the petitioner, filed with the court, and served on the respondent. See Exhibit p. 7. Mr. Sutton also suggests strengthening existing warnings as an alternative to the proposed law. See Exhibit p. 3.

It is unclear how effective a notice form would be in changing the behavior of those who divorce without revoking nonprobate transfers to a former spouse. Nor would such a warning help where a divorcing party is unaware of or has forgotten the existence of an instrument making a nonprobate transfer (as noted by Ms. Ratzlaff), or where a divorcing party dies after a status-only divorce, but before property division.

Although the staff is skeptical about the efficacy of a notice form alone, the Commission should consider whether such a notice would be an adequate alternative to the proposed law.

BURDEN ON MARRIED PERSONS

One of the chief concerns of CLTA is that, in order to protect those who divorce carelessly, the proposed law will impose burdens on those who remain married. See Exhibit p. 8. This is an important point, and the staff agrees that a rule protecting those who divorce at the expense of those who remain married would not be good policy. The potential burden on persons who remain married and measures to lighten that burden are discussed below.

Proof of Surviving Spouse Status

The proposed law provides that a nonprobate transfer to a former spouse fails if the former spouse is not the transferor's surviving spouse at the time of the transferor's death. CLTA wonders how a surviving spouse will demonstrate that they are in fact a surviving spouse, as such a demonstration requires the proof of a negative — that the surviving spouse and the decedent were not divorced. Such difficulty in demonstrating surviving spouse status might impede a nonprobate transfer to a surviving spouse.

This problem is avoided by means of the property holder protection provision. See proposed amendment to Probate Code Section 5003. Under that provision, a property holder may transfer property according to the terms of an instrument making a nonprobate transfer without incurring liability, even if the person named as beneficiary in the instrument is not the person entitled to the property under the

proposed law. This protection applies unless the property holder is served, before transferring the property, with a contrary court order or with written notice of a person claiming an adverse interest in the property. Thus, in an uncontested case, a surviving spouse will not need to prove surviving spouse status in order to receive property held by a third person.

CLTA has a problem with the drafting of the proposed amendment of Section 5003, which provides in part:

> 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, and whether or not the transfer has failed by operation of Section 5600.
>
> …

CLTA feels that protection of a transfer where the "transfer has failed" is a *non sequitur*. **As a drafting clarification, the staff proposes the following language:**

> 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, and whether or not the transfer is consistent with the rights of a person designated as beneficiary.
>
> …
>
> **Comment.** Section 5003(a) is amended to provide that the section applies where the rights of a former spouse designated as beneficiary to a nonprobate transfer are affected by operation of Section 5600.

Status of Title to Real Property

A more difficult problem involves the status of title to real property once it has been transferred. Because an apparent surviving spouse may not actually be a surviving spouse (because of an undisclosed divorce), an apparent surviving spouse may claim title to real property to which that person is not entitled under the proposed law. Consequently, the validity of title to all real property transferred by operation of a nonprobate transfer or joint tenancy survivorship would be cast

into doubt. Before insuring title to such property, a title insurer would need to research the marital status of the transferee to determine whether the transferee was the transferor's spouse at the time the instrument effecting the transfer was created and if so, whether the transferee was the surviving spouse of the transferor at the time of the transferor's death. Such research might be expensive and inconclusive, and might lead title insurers to refuse to insure title to such property. See Exhibit, pp. 5-7. This might make it more difficult for an actual surviving spouse to sell or encumber real property received from a former spouse by operation of a nonprobate transfer or joint tenancy survivorship.

The proposed law addresses this problem by protecting subsequent purchasers or encumbrancers for value in good faith who lack knowledge of the failure of a nonprobate transfer or the severance of a joint tenancy by operation of the proposed law. See proposed Sections 5600(d), 5601(c). Thus, the interests of a person who purchases real property from an apparent surviving spouse are protected if that person is unaware of an event that terminated the seller's status as surviving spouse.

CLTA finds this protection inadequate. Because the protection is conditioned on a question of fact (whether or not the third party knew that the transferee was not the transferor's surviving spouse), there is the potential for litigation between the transferor's heirs and the purchaser. Even if the purchaser prevails in such litigation, the insurer will still have incurred the costs of defending the title. This could increase the cost of insuring title to real property transferred by means of a nonprobate transfer or joint tenancy survivorship.

Proposed Solution

CLTA suggests, at Exhibit p. 8, the addition of a provision

> that allows any third party to rely absolutely upon a certificate executed under penalty of perjury from the surviving spouse stating that he/she was married to the decedent at the date of death. The provision would also state [that] there is no duty of inquiry by any third party.

This seems reasonable. Similar affidavit procedures govern succession to real property of small value (see Prob. Code § 13200 *et seq.*) and may be used in the disposal of community or quasi-community real property by a surviving spouse. (see Prob. Code § 13540 *et seq.*). **The staff proposes the addition of the following section:**

§ ____. Affidavit regarding status as surviving spouse

____. (a) Nothing in this part affects the rights of a purchaser or encumbrancer of real property for value in good faith who relies on an affidavit or a declaration under penalty of perjury under the laws of this state that states all of the following:

(1) The name of the decedent.

(2) The date and place of the decedent's death.

(3) The affiant or declarant is the surviving spouse of the decedent.

(4) Either of the following, as appropriate:

(A) The affiant or declarant is entitled to real property transferred on the decedent's death pursuant to an instrument designating the affiant or declarant as beneficiary.

(B) The affiant or declarant has title by right of survivorship to the decedent's interest in real property held in joint tenancy between the affiant or declarant and the decedent.

(b) A person relying on an affidavit or declaration made pursuant to subdivision (a) has no duty to inquire into the truth of the matters stated in the affidavit or declaration.

(c) An affidavit or declaration made pursuant to subdivision (a) may be recorded.

Comment. Section ____ provides a procedure for certifying a surviving spouse's rights under this part. See also Civ. Code Proc. § 2015.5 (certification or declaration under penalty of perjury); Prob. Code §§ 210-212 (recording evidence of death affecting title to real property).

The procedure set out above is intended as a quick and simple means of certifying a surviving spouse's rights under the proposed law. **The Commission may wish to consider elaborating on this procedure in order to reduce the likelihood of fraud.** For example, the procedure could require attachment of a certified copy of a death certification or could impose a waiting period before the transferee could dispose of the property. This would provide time for a person with a contending claim to assert that claim.

EFFECT ON EXISTING INSTRUMENTS

Both CLTA and the Executive Committee have concerns regarding proposed Section 5602 (application of part). That section provides that the proposed law would be operative January 1, 2000, but would not affect a nonprobate transfer or joint tenancy created before the operative date (erroneously identified as January 1, 1999, in proposed Section 5602(b)) if the transferor or joint tenant dies before

January 1, 2002. This limitation on the application of the proposed law to preexisting nonprobate transfers has two effects:

> (1) Nonprobate transfers that are completed by the death of the transferor before the operative date of the new law are unaffected by the new law.
>
> (2) Where a nonprobate transfer was created before the operative date of the proposed law, transferors have a two-year grace period during which they may change the terms of the transfers, if they wish to do so.

Retroactive Application

CLTA questions whether it is fair to apply the proposed law retroactively, given that it will frustrate the intentions of a divorcing party who relied on then-existing law in settling a divorce, "merely to protect those persons who fail to take prudent action to revoke transfers when they are involved in a divorce." See Exhibit p. 7. For this reason, CLTA suggests that the law should not have retroactive effect.

The staff concedes that the proposed law would be unfair to those who divorced before the operative date of the new law and intended to preserve a nonprobate transfer to a former spouse. The question is whether this unfairness is sufficiently outweighed by the benefit of retroactive application of the proposed law — the protection of the presumably larger group of those who did not intend to preserve a nonprobate transfer to a former spouse. This question does not have a clear answer, and **the Commission should consider whether to limit the proposed law's application to nonprobate transfers and joint tenancies created after the operative date of the proposed law.**

Incapacity During the Grace Period

Proposed Section 5602(b) provides that the proposed law does not apply to a preexisting nonprobate transfer if the transferor dies within the first two years of the proposed law's operation. This mitigates the potential unfairness of retroactive application of the proposed law, by providing a grace period during which a nonprobate transfer can be modified or reaffirmed to take the new law into account.

The Executive Committee is concerned that an incapacitated person will not be able to take advantage of this grace period. See Exhibit pp. 9-10. Of course, we can assume that most incapacitated people, like most people generally, would not

intend a nonprobate transfer to a former spouse to continue after divorce. Therefore, the interests of most incapacitated people would be served by application of the proposed law, despite their inability to take advantage of the grace period.

The basic policy question is really the same as that raised by CLTA and discussed above — is it fair to apply the proposed law retroactively, protecting most people's intentions, given that the intentions of those who intend to preserve a nonprobate transfer to a former spouse will be frustrated? If the Commission decides that the unfairness of retroactive application of the proposed law outweighs the benefit of retroactive application, then the law should be made prospective only. If, on the other hand, the Commission believes that the benefit of retroactive application outweighs the unfairness to those who intend to preserve a nonprobate transfer to a former spouse, then the law should apply retroactively to all, including those who do not know about the change in the law or lack the capacity to act to protect their intentions during the grace period.

However, the Commission may conclude that the opportunity to change a nonprobate transfer during the grace period is what tips the balance in favor of retroactive application. In that case, the transitional provision should perhaps be revised along the general lines suggested by the Executive Committee at Exhibit p. 10:

> 5602. (a) This part is operative January 1, 2000.
> (b) This part does not affect a nonprobate transfer or joint tenancy created before January 1, 2000, if the transferor or joint tenant dies <u>or becomes or is incapacitated</u> before January 1, 2002.

The drafting of a such a provision would need to be somewhat more complex, however. For example, the Commission would need to consider each of the following points:

> *Nature of incapacity*. What standard should be used to determine incapacity in this context? Possible standards include the incapacity to make decisions (see Prob. Code § 812), sufficient incapacity to support the appointment of a conservator of the estate (see Prob. Code § 1801(b), or a lack of testamentary capacity (see Prob. Code § 6100.5).
>
> *How would incapacity be proven?* Should the determination be required before the person has died or could a former spouse prove the incapacity of a transferor after the transferor's death? The latter

would introduce more uncertainty and would probably result in more litigation.

Duration of incapacity. Should the duration of the incapacity matter? What should the result be where a person is incapacitated or becomes incapacitated during the grace period, then recovers capacity before the end of the grace period? This situation would probably be relatively rare, but should probably be accounted for in some way.

On balance, the staff recommends against a provision accounting for incapacity during the grace period. If the unfairness of retroactive application is significant enough to outweigh the benefit of retroactive application, the law should be made prospective only.

EFFECT ON TRUSTEE

CLTA asks whether the proposed law would revoke the status of a former spouse as trustee, as well as revoking their status as trust beneficiary. See Exhibit p. 7. As currently drafted it would not. Neither would it affect an instrument conferring a revocable power of appointment on a former spouse.

Under existing law divorce automatically revokes such provisions in a will. See Prob. Code § 6122(a)(2) & (3) (revocation of provision of will conferring power of appointment on former spouse or naming former spouse as trustee). **Therefore, it probably makes sense to expand the application of the proposed law to affect powers of appointment and the naming of trustees.** The same policy assumption applies — a divorcing person who does not intend to preserve a nonprobate transfer of property to a former spouse probably does not intend to preserve an arrangement entrusting the disposition or management of property to a former spouse.

A rule terminating a provision conferring a power of appointment on a former spouse or naming a former spouse as trustee could be added by revising proposed Section 5600 to read as follows (changes from tentative recommendation draft are indicated in strikeout and underscore):

§ 5600. Failure of nonprobate transfer to former spouse

5600. (a) Except as provided in subdivision (b), a nonprobate transfer to the transferor's former spouse, in an instrument executed by the transferor before or during the marriage, fails if, at the time of the transferor's death, the former spouse is not the transferor's surviving spouse.

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

(1) The nonprobate transfer is not revocable by the transferor immediately prior to the transferor's death.

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

(c) Where a nonprobate transfer fails by operation of this section, ~~the property is instead transferred pursuant to Section 21111~~ the instrument making the nonprobate transfer shall be given effect as if the former spouse failed to survive the transferor.

(d) Nothing in this section affects the rights of a subsequent purchaser or encumbrancer for value in good faith who relies on the apparent failure of a nonprobate transfer under this section or who lacks knowledge of the failure of a nonprobate transfer under this section.

(e) As used in this section, "nonprobate transfer" means a provision that operates on death, of either of the following types:

(1) A provision of a type described in Section 5000 for a transfer of property ~~on death~~.

(2) A provision conferring a power of appointment or naming a trustee.

Note that subdivision (c) is changed slightly to account for the application of the section to trustee designations. The revised provision would treat a failed transfer as if the transferee had predeceased the transferor. For transfers of property (including, presumably, property transferred under a power of appointment) this would still trigger the application of Section 21111.

For the failure of a trustee designation, the provision would trigger Probate Code Section 15660, governing the appointment of a new trustee where a trust has no trustee. Section 15660 looks first to the trust instrument for a means of filling a vacancy in the office of trustee. If the instrument does not provide a practical method for filling the vacancy, the beneficiaries may accept appointment of a trust company as trustee. If neither of these alternatives result in the appointment of a replacement trustee, any interested person may petition the court to appoint a trustee.

PROVING IRREVOCABILITY OF A TRUST

Under the proposed law a nonprobate transfer does not fail if the nonprobate transfer is irrevocable. CLTA wonders how the irrevocability of a trust would be proven, considering that many people wish to keep the precise terms of a trust

private. See Exhibit p. 7. The general mechanism for establishing the terms of a trust is certification by the trustee. See Prob. Code § 18100.5 (certification of trust).

CLTA also asks whether there would be any problem relying on certification by a trustee who is also a beneficiary of the trust. See Exhibit p. 7. The staff can see two problems that could arise in such a situation:

> (1) The beneficiary-trustee might intentionally or inadvertently misrepresent the terms of the trust.
>
> (2) The beneficiary-trustee might be barred from acting as trustee by operation of the proposed law (see previous discussion).

The first possibility is accounted for in Probate Code Section 18100.5(f), which protects "a person who acts in reliance upon a certification of trust without actual knowledge that the representations contained therein are incorrect." The second problem is accounted for in Probate Code Section 18102, which provides:

> If a third person acting in good faith and for a valuable consideration enters into a transaction with a former trustee without knowledge that the person is no longer a trustee, the third person is fully protected just as if the former trustee were still a trustee.

Consequently, a third person should have no problem relying on a beneficiary-trustee's certification of the revocability or irrevocability of the trust.

The staff recommends adding language to the Comment to proposed Section 5600 to refer to the provisions protecting a third party who relies on a trustee's certification of the contents of a trust.

Note that the current draft uses somewhat convoluted language to refer to an instrument's irrevocability: "the nonprobate transfer is not revocable by the transferor immediately prior to the transferor's death." This formulation was adopted to make clear that our use of the term irrevocable was not intended to encompass irrevocability resulting from the transferor's death. It seems that this could be communicated just as effectively in the Comment, without resorting to such contorted language in the statute. **The staff recommends using more straightforward language in proposed Sections 5600(b)(1) and 5601(b)(1), and adding clarifying language to the Comments.**

EXPRESS OPT-OUT LANGUAGE

At Exhibit p. 8, CLTA proposes that

> statutory language be drafted which, if added to a nonprobate transfer at the date of creation, will supersede entirely the Proposed Law thereby making the transfer absolute unless revoked by the transferor in a separate written instrument.

The staff recommends against such a provision. The proposed law affects nonprobate transfers created during marriage. At that time, most people will not be contemplating divorce. Consequently a statement of intention at the time of the creation of a nonprobate transfer would probably not reflect a person's intentions at the time of a subsequent divorce. What's more, the statutory exemption language might be adopted as boilerplate in standardized instruments making nonprobate transfers. This would substantially undermine the benefit of the proposed law.

EVIDENCE OF CONTRARY INTENT

The proposed law does not apply to a nonprobate transfer if there is clear and convincing evidence that the transferor intended the transfer to a former spouse to continue after divorce. Mr. Fulton questions the use of the clear and convincing evidence standard in this exception. See Exhibit p. 1. The purpose of this standard is to allow evidence of a contrary intent to override the proposed law's default rule without opening the door to a flood of litigation. Such litigation would undermine the value of a nonprobate transfer as a relatively simple and inexpensive way to transfer property on death.

While it may seem that the evidentiary standard is too strict, it actually creates an exception that is more liberal than the exceptions available in similar provisions of existing law. For example, the only exceptions to the rules providing that divorce revokes a will provision benefiting a former spouse or a durable power of attorney for health care naming a former spouse as attorney-in-fact are where revocation on divorce is contrary to an express provision in the relevant instrument. See Prob. Code §§ 4727 (durable power of attorney for health care), 6122 (will). Other statutes revoking a nonprobate transfer to a former spouse on divorce contain no intent-based exceptions whatsoever. See Gov't Code § 21492 (PERS death benefits); Prob. Code §§ 3722 (power of attorney of federal absentee), 4154 (power of attorney generally).

Note too that there are other provisions of the Probate Code that apply the clear and convincing evidence standard when considering evidence of an intent contrary to a statutory default rule. See, e.g., Prob. Code §§ 5301 (lifetime

ownership of funds in joint account), 5302 (disposition of funds in joint account on death of one account-holder).

The staff recommends no change to the tentative recommendation on this point.

Respectfully submitted,

Brian Hebert
Staff Counsel

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February 20, 1998

California Law Revision Commission
Attn: Brian Hebert
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Palo Alto, CA 94303-4739

Re: Effect of Dissolution of Marriage on Nonprobate Transfers

Dear Mr. Hebert:

Likely this and many other pro or con comments have been received in regard to the Commission's tentative recommendation concerning the effect of a dissolution of marriage on a revocable nonprobate transfer to a former spouse upon death of the transferror. I have three to add to the stack:

(1) The law cannot protect us from everything. Recall Pogo's admonition, "We has met the enemy and they is us!"

(2) What data supports the idea a person making a nonprobate transfer "probably does not intend that it continue to operate in favor of the spouse after dissolution of marriage."

Is it reasonable to believe that at the time a person makes such a transfer he/she intends to later dissolve the marriage? Should our law contemplate all married persons will dissolve their marriages? Would a provision such as this proposed law be enforceable if included as a term in a California premarital agreement?

(3) "Clear and convincing?" Why the high standard? The tentative recommendation contains no discussion of why this level of evidence should be required. There ought to be.

Unfortunately, this proposal epitomizes law making today ... some call it "micro managing" society. I think it is more an "*in parens patriae* legislative attitude that assumes an ignorant, unintelligent populous needs job instruction level laws to conduct its daily affairs. I suppose my base inquiry really is "How did we ever get to where we are without this kind of help?"

My recommendation, work on repealing laws ... do not add to a body of law already beyond the comprehension of anyone.

Finally, does this tentative recommendation get routinely distributed to the probate and family law sections of the various bar associations? If not, it should.

Very truly yours,

Robert J. Fulton
Certified Family Law Specialist

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February 24, 1998

California Law Revision Commiss. Via Fax (650) 494-1827
Attn: Brian Hebert Ph (650) 494-1335
4000 Middlefield Road, Room D-1
Palo Alto, CA 93403-4739

Re: Proposed Law re Nonprobate Transfers

Dear Mr. Hebert,

I write to oppose the proposed new statute which would say that a nonprobate transfer, such as joint tenancy, is presumed to be rendered invalid by a subsequent dissolution of marriage order which is silent on the property.

I practice real estate law and believe that 400 years of Common Law teaches us that record title is important and should be reliable. A joint tenancy can be unilaterally and cheaply severed by a recorded deed to oneself as tenant in common. Why do you want to render uncertain all joint tenancy titles on the chance that one of the parties will subsequently get divorced and be too dumb to clarify title?

You must assume that every divorce lawyer is incompetent, or that every party will save a "few dollars" and act as his/her own divorce attorney and not sever the joint tenancy. The first assumption is not true, and the second only results in personal responsibilty for personal decisions. Either assumption does not justify the expense and disruption that will result if no lender or title insurer can rely on apparent, record title without exploring the secret intentions and marital happiness of the parties. You should be acting to promote and protect the status of apparent, record title, not undermining it.

If a divorcing person leaves a former spouse as the surviving joint tenant on real property, so be it. He/she should have hired an attorney. The courts can declare a constructive trust in the few appropriate cases. The better remedy is to divorce correctly. Put a warning in the divorce judgment form.

Very truly yours,

M. Dean Sutton

sccbarp.007

cc: Dan Ballesteros, Esq. Via Fax (408) 287-2583
Chair, SCCBA Real Property Committee

TOTAL P.01

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February 23, 1998

California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303

Re: Effect of Dissolution of Marriage on Nonprobate Transfers

Dear California Law Revision Commission:

I have reviewed your tentative recommendation on proposed changes to California law related to the effect of dissolution of marriage on nonprobate transfers. I wholeheartedly support the recommended changes.

I have practiced in the area of estate planning and probate for over 18 years. In cases where there has been a dissolution of the marriage, a thorough estate planning attorney should spend time inquiring about the types of matters your proposal addresses. Clients aren't always interested in paying for the attorney's time and frequently feel that the dissolution took care of all such issues, particularly since it is so clearly stated in the Judicial Council forms that a will is revoked upon dissolution.

Often the insurance policies or beneficiary designations appear so inconsequential when they are initiated that clients can forget that life insurance was a component of a credit union account, for example.

I support the Commission's recommendation that the law be applied broadly and not be limited to contracts formed after the law's enactment. Consequently, there doesn't seem to be a need for the proposed two-year grace period. Lay people who don't attend to business are not going to be aware the change has been made let alone take the steps necessary to preserve an existing nonprobate transfer or joint tenancy benefiting a former spouse.

Sincerely,

Ruth E. Ratzlaff

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Anne Nelson Lanphar
Vice President
Associate Senior Underwriter

VIA FEDERAL EXPRESS

April 29, 1998

California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

Re: Response of CLTA to California Law Revision Commission - Effect of Dissolution of Marriage on Nonprobate Transfers

Dear Ladies and Gentlemen:

I am writing to you on behalf of the California Land Title Association ("CLTA") which is an industry association of title companies in California.

This letter will serve as the official response and comments of the CLTA to the document entitled "Effect of Dissolution of Marriage on Nonprobate Transfers" drafted by the California Law Revision Commission dated January 1998 ("Proposed Law"). The CLTA is very concerned with the potential impact of the Proposed Law upon future nonprobate transfers.

California law currently provides that the dissolution of a marriage automatically revokes a disposition made to the former spouse in a will. The purpose of the Proposed Law is to create a similar automatic revocation of nonprobate transfers (i.e. joint tenancy, trusts, pensions, insurance, etc.) to a former spouse upon dissolution of marriage.

Although the purpose is laudable, the Proposed Law will create serious adverse impacts on those surviving spouses who are married at the date of death. Upon the death of a spouse, the surviving spouse will have to ***affirmatively*** prove to title insurance companies, life insurance companies, etc. that they were, in fact, married at the date of death. How do you prove that you are <u>not</u> divorced? Since there is no single governmental registry that provides such information, this will create a difficult, if not impossible, burden on a surviving spouse. The "safe harbors" in the Proposed Law (Section 5600(d) and Section 5601(b)(2)) are not

sufficient because they are conditional. Section 5600(d) is conditioned upon a "lack of knowledge" by the third party, which, by definition, creates a question of fact. Also, does the third party have a duty of reasonable inquiry? In the situation where the parties are divorced, the Proposed Law creates the problem of forcing the third party to be the arbiter of a question of fact as to whether there is "clear and convincing evidence" of the intent of the decedent (Section 5601(b)(2)). Therefore, the ultimate effect of the Proposed Law will be to protect divording parties at the expense of married persons who will now have the burden to show that the nonprobate transfers remain valid. This situation will effectively undermine all nonprobate transfers.

The existing law which automatically revokes transfers in wills does not create similar issues because a will is administered through a judicial action wherein the interests of all parties are protected by the court. The Proposed Law will create an unfair burden on married couples for the benefit of divorcing couples who should be responsible to revoke any undesired transfers. The divorcing couples can *act* to protect themselves - the married couple now has an onerous burden upon death merely because they were married! The Proposed Law places the third parties (i.e. title insurance company, the life insurance company, bank, etc.) in the untenable position of trying to determine the facts and circumstances for *each and every* nonprobate transfer which will, of course, result in increasing the cost and expense to these companies. Despite the "safe harbors," the ultimate reality of the situation is that these companies will not want to be dragged into lawsuits over these types of transfers which **will** undoubtedly occur. For example, a title policy issued to a buyer of real property where the seller is a surviving spouse who acquired title by trust or by joint tenancy will, by definition, have a significantly higher risk of a lawsuit from disgruntled heirs of the seller. The "safe harbors" are not an absolute barrier because if there is a subsequent judicial determination that the title company had some "knowledge" or "duty to inquire," the reality is that there will be a **total failure of title** (which is a title insurer's worst nightmare) and both the buyer and the buyer's lender will have the right to claim the full amount of the policy limits. (Although the title company will be subrogated to insured's rights against the seller, as a practical matter, this is **not** an effective remedy.) The "safe harbor" proposed in Section 5003 is ambiguous at best, since it states that despite the "failure" of the transfer under Section 5600, the transferee has authority to transfer the property. How can the person transfer property when the transfer to him/her has failed? This does not make sense: it is a *non sequitur*! Furthermore, assuming that a judicial determination ultimately upholds the validity of the nonprobate transfer, these types of transfers will create a significant problem for title insurers because the obligation of defense under the title policy is independent from the indemnity obligation, and the *increased risk of claims* for nonprobate transfers may very will result in the situation where title companies

will elect not to insure such transfers without some sort of judicial determination (i.e. quite title action or other procedure) which confirms the vesting of title in the surviving spouse. Obviously, nonprobate transfers will become more risky, time consuming and expensive than probate transfers, thereby effectively undermining nonprobate transfers entirely.

Another problem under the Proposed Law is that not all divorces are, in fact, adversarial and, furthermore, some property settlements include obligations that survive death. Query: what happens to existing marital dissolution settlement agreements which contemplate and mandate that certain transfers remain in effect even at death such as life insurance policies naming the former spouse as the beneficiary, pension plans naming the former spouse as the beneficiary, etc.? Although there is a time lapse before the law becomes effective, existing settlement agreements which have such transfers may be called into question. Accordingly, these situations are made very difficult if not impossible merely to protect those persons who fail to take prudent action to revoke transfers when they are involved in a divorce.

Although Section 5600(b)(1) of the Proposed Law indicates that transfers to an irrevocable trust are not to be deemed revoked, consideration should be given to the practical problems that will occur in the trust situation. Besides a spouse being a beneficiary of a revocable trust, often the surviving spouse is also named as the trustee of the trust. Query: is that appointment, as trustee, also to be automatically revoked? In order to determine whether the trust was revocable or irrevocable, the title company will have to review the trust instrument which the parties generally want to keep private. Generally the person providing the documents to the third party will be the trustee/surviving spouse! Query: can the third party rely upon certification from the trustee/surviving spouse?

We propose a complete alternative to the Proposed Law: rather that nonprobate transfers being automatically revoked, protect divorcing parties by adding a <u>separate</u> Judicial Council form to the dissolution process that gives notice to both parties warning the parties to consider modifying nonprobate transfers. This warning form (containing language substantially the same as in proposed Section 2024) could be required to be executed by the petitioner and filed with the court and a copy of the same form served on the respondent. These forms could be a mandatory part of the dissolution proceedings. This process would remind the parties to consider the nonprobate transfers thereby protecting divorcing couples from forgetting and inadvertently passing property to the spouse and still protect the integrity of nonprobate transfers in California as an effective estate planning tool for married couples.

We do not support the Proposed Law for the reasons stated above and believe that the warning form will be sufficient to remind divorcing parties to take appropriate action. However, if the Proposed Law is to be adopted, we strongly recommended the following changes:

- that a provision be added to the law that allows any third party to rely absolutely upon a certificate executed under penalty of perjury from the surviving spouse stating the he/she was married to the decedent at the date of death. The provision should also state that there is no duty of inquiry by any third party.
- statutory language be drafted which, if added to a nonprobate instrument at the date of creation, will supersede entirely the Proposed Law thereby making the transfer absolute unless revoked by the transferor in a separate written instrument.
- the Proposed Law should not be effective for existing nonprobate transfers. Rather the law should apply only to nonprobate transfers created after a certain date.

In summary, we believe that the Proposed Law will completely undermine the integrity of nonprobate transfers making them more difficult and expensive than probate transfers. The practical consequence of the Proposed Law is to unfairly shift responsibility for protecting certain members of society: ***from*** those who are actively involved in a dissolution and who should be responsible (with their legal counsel) to effect revocation of such nonprobate transfers as a part of their dissolution ***to*** those who are married hoping to effect their last wishes through proper estate planning with the expectation that such planning will reduce or eliminate unnecessary burdens on their surviving spouse.

Thank you for considering our comments. If I can be of any further assistance to you, please do not hesitate to contact me.

Very truly yours,

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MEMORANDUM

TO: California Law Revision Commission
[via facsimile (650) 494 1827]

FROM: Executive Committee, Estate Planning, Trust & Probate Section, State Bar of California

RE: Effect of Dissolution of Marriage on Nonprobate Transfers

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The Executive Committee, Estate Planning, Trust & Probate Section, State Bar of California (the "Executive Committee") supports the recommendation of the California Law Revision Commission ("CLRC") that a judgment of dissolution or annulment of marriage should prevent the operation of a revocable nonprobate transfer on death to a former spouse. The Executive Committee believes that said recommendation reflects the likely intent of the parties to a dissolution or annulment.

Nevertheless, the Executive Committee believes that proposed Probate Code §5602, which provides the transitional rules, be modified to include those persons who become incompetent during the transitional period.

* * * *

Under the legislation as proposed, if a person dies during the transitional period, the former law would apply to the transfer of property to a former spouse and the former spouse ***would*** inherit the property. On the other hand, if a person were instead to become incompetent during the same period, or was already incompetent prior to the effective date, the ***new*** law would apply and the former spouse ***would not*** inherit the property.

Those persons who will become incompetent during the transitional period, or are already incompetent, stand in the same position as those persons who will die during that same period: none will have the opportunity to change their estate plans to reflect the new law.

While it is true that a conservator or former spouse would be free to seek a court order to bring back the effect of the old law, such would require the time and expense involved in not only the appointment of a conservator but a special proceeding to invoke the "substituted judgement" powers of the court. Moreover, such an order would need to be obtained ***prior*** to the death of the incompentent person, which may be ***after*** the existence of the non-probate asset is determined.

Therefore, we suggest that proposed Probate Code Section 5602 read as follows:

> §5602.(a) This part is operative January 1, 1999. (b) This part does not affect a nonprobate transfer or joint tenancy created before January 1, 1999, if the transferor or joint tenant dies or becomes or is incompetent before January 1, 2002.

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cc: Mr. Robert E. Temmerman, Chair, Estate Planning, Trust and Probate Law Section
Mr. Don Green, Immediate Past Chair, Estate Planning, Trust and Probate Law Section
Mrs. Diana Hastings Temple, Chair, Ad Hoc Subcommittee
Mr. Richard A. Gorini
Mr. Lynard C. Hinojosa
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