

## Memorandum 2000-51

### **Estate Planning During Dissolution of Marriage (Draft of Recommendation)**

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At its June meeting, the Commission considered public comments on its tentative recommendation relating to *Estate Planning During Marital Dissolution*, which would clarify the effect of the automatic temporary restraining order (ATRO) that is in effect during a proceeding for dissolution or annulment of marriage. The Commission instructed the staff to prepare a draft recommendation based on the tentative recommendation. The draft recommendation is attached. The Commission should review that draft and decide whether to approve it as its final recommendation.

The Commission also indicated its interest in receiving additional public comment on two issues:

#### **Restraint of Unfunded Living Trust**

The Commission received a comment suggesting that the ATRO should restrain the transfer of property to a living trust during a dissolution proceeding, but should not restrain the creation of an unfunded living trust. An unfunded living trust could serve as a receptacle for property subject to a pour-over provision in a will. Considering that such property would be subject to probate administration (unless otherwise excepted), the staff is unsure what the benefit of such an arrangement would be. The Commission would like to receive additional comment on the benefit of creating an unfunded living trust during dissolution of marriage.

#### **Restraint on Modification of Nonprobate Transfer**

The Commission decided to limit the restraint on modification of a nonprobate transfer to those modifications that affect disposition of property subject to the transfer. See attached draft, pp. 4-5, 7-8. The following language was added to the Comment to help clarify the scope of the restraint:

Subdivision (a)(4) restrains modification of a nonprobate transfer "in a manner that affects the disposition of property." Modifications that are restrained as affecting the disposition of

property include a change of beneficiary or power of appointment. Modifications that are not restrained include naming a new trustee or successor trustee (so long as the change does not affect the trustee's powers or duties with respect to disposition of trust property).

The Commission would like to receive comment on the proposed limitation.

Respectfully submitted,

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## ESTATE PLANNING DURING MARITAL DISSOLUTION

1 Existing law imposes an automatic temporary restraining order (ATRO) on both  
2 parties in a proceeding for dissolution or annulment of marriage, or legal  
3 separation (hereinafter “dissolution”). Except as necessary to pay attorney’s fees  
4 or ordinary expenses, the ATRO restrains the parties from “transferring,  
5 encumbering, hypothecating, concealing, or in any way disposing of any property,  
6 real or personal, whether community, quasi-community, or separate, without the  
7 written consent of the other party or an order of the court.”<sup>1</sup> The extent to which  
8 the ATRO restrains estate planning changes during a dissolution proceeding is not  
9 clear. The Commission has been informed that different trial courts interpret the  
10 ATRO differently — some interpret the ATRO as restraining estate planning  
11 changes while others do not.<sup>2</sup>

12 In a recent decision, *Estate of Mitchell*, the court held that revocation of a joint  
13 tenancy is not restrained by the ATRO, because unilateral severance does not  
14 involve a transfer and because severance only disposes of an expectancy, not  
15 property.<sup>3</sup> This is a reasonable interpretation of Family Code Section 2040.  
16 However, the opinion does not consider other types of estate planning changes,  
17 such as creation, modification, or revocation of a trust. The applicability of the  
18 ATRO to these other types of changes should also be clarified.

### PROBLEMS WITH EXISTING LAW

#### 19 **Uncertainty**

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21 Uncertainty as to whether the ATRO restrains estate planning changes can create  
22 a trap for unwary parties and inexperienced practitioners. For example, if a party  
23 makes an estate planning change during a dissolution proceeding without first  
24 obtaining spousal consent or the permission of the court, and the court interprets

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1. See Fam. Code § 2040(a)(2).

2. This uncertainty is reflected in a standard family practice treatise and in a recent publication of the California State Bar Family Law Section. See W. Hogoboom & D. King, *California Practice Guide: Family Law* ¶ 1:394.1 (1999) (cautioning that severance of a joint tenancy “may well” violate the ATRO); Moore, *Selected Estate Planning Issues for Family Lawyers*, *Family Law News*, California State Bar Family Law Section, Winter 1996, at 12-13 (discussing uncertainty as to whether ATRO applies to severance of joint tenancy and revocation of trust).

Courts in other states have interpreted similar provisions restraining the disposal of property during a marital dissolution proceeding, with varying results. See, e.g., *Lindsey v. Lindsey*, 492 A.2d 396 (Pa. Super. 1985) (change of beneficiary designation on life insurance policies not conveyance of asset because beneficiary designation vests nothing in beneficiary during lifetime of insured — beneficiary has mere expectancy); *Lonergan v. Strom*, 700 P.2d 893 (Ariz. 1985) (severance of joint tenancy by means of straw transfer violated ATRO, but did not violate purpose of ATRO — to protect marital estate from dissipation or removal beyond reach of divorce court); *Willoughby v. Willoughby* 758 F. Supp. 646 (DC Kan. 1990) (change of life insurance beneficiary was disposition of property in violation of restraining order). See generally Chapus, *Divorce and Separation: Effect of Court Order Prohibiting Sale or Transfer of Property on Party’s Right to Change Beneficiary of Insurance Policy*, 68 A.L.R.4th 929 (Westlaw 1999).

3. *Estate of Mitchell*, 76 Cal. App. 4th 1378, 91 Cal. Rptr. 2d 192 (1999).

1 the ATRO as restraining such a change, the change may be ineffective and the  
2 party may be held in contempt.<sup>4</sup>

### 3 **Unintended Transfers**

4 A change in a person's life as significant as dissolution of marriage will often  
5 lead to changes in that person's testamentary intentions. If the ATRO prevents a  
6 person from making an intended estate planning change and the person dies during  
7 the dissolution proceeding, the person's estate will pass in an unintended way. For  
8 example, suppose a husband and wife convey their community property into a  
9 trust that names the survivor of them as beneficiary and is unilaterally revocable  
10 by either. The wife later files for dissolution of marriage and decides to revoke the  
11 trust and execute a will devising her share of the community property to her  
12 children. Before she can obtain a court order permitting the estate planning  
13 changes, she dies, and contrary to her wishes, her husband receives the entire  
14 property.

### 15 **Inefficiency**

16 It appears that a principal purpose of the ATRO provision is to conserve judicial  
17 resources by making automatic those types of restraints that are commonly sought  
18 and granted in dissolution proceedings.<sup>5</sup> However, if parties to a dissolution  
19 routinely wish to make estate planning changes during the proceeding, then  
20 judicial efficiency is not served by an automatic restraint of such changes. In fact,  
21 estate planning changes during dissolution of marriage appear to be commonplace.  
22 In one appellate decision, the court suggests that family law attorneys risk  
23 malpractice liability if they do not advise their clients of the need to make estate  
24 planning changes during a dissolution proceeding in order to avoid an unintended  
25 transfer if the client dies during the proceeding.<sup>6</sup> Similar advice is provided in  
26 standard family law practice treatises.<sup>7</sup> Considering that careful attorneys will seek

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4. See Civ. Code § 2224 (“One who gains a thing by ... wrongful act, is ... an involuntary trustee of the thing gained, for the benefit of the person who would otherwise have had it.”); Code Civ. Proc. § 1209(a)(5) (contempt includes disobedience of lawful court order).

5. See, e.g., Assembly Committee on Judiciary analysis of Assembly Bill 1905, May 4, 1989, at 6:

Proponents state that the restraining orders contained in this proposal are granted routinely by courts following the filing of an Order to Show Cause (OSC). One of the elements presently contributing to court congestion in family law courts is the routine filing of such OSC's simply to obtain these standard orders, with the attendant court time necessary for perfunctory hearings or, as is usual, signing in chambers. One or both parties usually seek at least one of these restraining orders soon after filing the family law action.

This proposal would save court time without diminishing the parties' right to a hearing. Either party always would have the option of filing a motion to request that the orders be dissolved.

6. See Estate of Blair, 199 Cal. App. 3d 161, 169, 244 Cal. Rptr. 627, 631 (1988).

7. See W. Hogoboom & D. King, California Practice Guide: Family Law ¶¶ 1:367-369, 390 (suggesting that it is the duty of family law attorneys to promptly inquire whether their clients wish to sever joint tenancy in order to avoid unintended transfer if client dies during proceeding); K. Kirkland et al., California Family Law Practice and Procedure § 20.12[4][a][iv] (2d ed. 1999) (suggesting that clients should be advised to sever joint tenancy on commencing family law proceeding in order to avoid possible

1 spousal consent or an order of the court before taking such actions, the court will  
2 be required to hear numerous requests that would be granted in many cases — an  
3 apparent waste of judicial resources.

4 **Disproportionate Effect on Respondent Spouse**

5 The ATRO takes effect on service of the summons in a proceeding for  
6 dissolution of marriage.<sup>8</sup> A petitioner can effectively avoid the ATRO by making  
7 any desired estate planning changes before filing. A respondent who is unaware of  
8 a pending summons cannot avoid the ATRO in this way. The problems associated  
9 with the ATRO provision disproportionately affect respondents.

10 **PROPER SCOPE OF RESTRAINING ORDER**

11 As a general matter, it is inequitable and inefficient to require that a party to a  
12 dissolution proceeding obtain spousal consent or an order of the court before  
13 making estate planning changes that do not affect the rights of the other spouse.  
14 Such a restraint also exceeds the proper purpose of the ATRO — protecting  
15 marital assets from dissipation or concealment. As stated in an Arizona case  
16 interpreting a similar ATRO provision:

17 In our opinion, it is not the purpose of [the ATRO] to freeze each party's estate  
18 plan as of the date of the filing of the petition for dissolution and thus insure that it  
19 will be effectuated without alteration in the event one of the parties dies before  
20 entry of a final decree. The statutory intent is to forbid actions by either party that  
21 would dissipate the property of the marital estate or place it beyond the court's  
22 adjudicatory power in the dissolution proceeding.<sup>9</sup>

23 Whether different types of estate planning changes might adversely affect the  
24 property interests of the other spouse is discussed below.

25 **Transaction Involving a Will**

26 The beneficiary of a will has no vested property interest in the will during the  
27 testator's life. Thus, a decision by one spouse to create, modify, or revoke a will  
28 during a dissolution proceeding does not affect the rights of the other spouse and  
29 should not be automatically restrained. This is consistent with the holding in  
30 *Estate of Mitchell*, that the ATRO does not restrain termination of an expectancy.<sup>10</sup>

31 Of course, spouses may agree by contract to make a particular testamentary  
32 disposition by will. In such a case, the contract itself serves to restrain

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unintended transfer to other spouse). Although these examples focus on joint tenancy survivorship, the same concerns are raised by other instruments that transfer property on death.

8. See Fam. Code § 233(a).

9. Lonergan v. Strom, 700 P.2d 893, 898 (Ariz. 1985).

10. See *supra* note 3.

1 modification or revocation of the agreed-upon will provision.<sup>11</sup> It is not necessary  
2 that all estate planning changes involving wills be automatically restrained during  
3 dissolution proceedings in order to protect these contractual agreements.

#### 4 **Revocation of Nonprobate Transfer**

5 Many people choose to use a “nonprobate transfer” (such as a revocable trust,  
6 joint tenancy title, or a pay-on-death (P.O.D.) account in a financial institution), in  
7 order to pass property on death outside of the probate process. Revocation of a  
8 revocable nonprobate transfer is similar to revocation of a will in that it terminates  
9 a mere expectancy.<sup>12</sup> There does not appear to be any reason to automatically  
10 restrain the revocation of a nonprobate transfer during a dissolution proceeding.<sup>13</sup>  
11 Again, this is consistent with the holding in *Estate of Mitchell*.<sup>14</sup>

#### 12 **Modification of a Nonprobate Transfer**

13 Modification of a nonprobate transfer during a dissolution proceeding can result  
14 in an unauthorized transfer of community property. This is because a nonprobate  
15 transfer, unlike a will, can be used to dispose of both spouses’ shares of the  
16 community property, so long as both spouses have consented to the transfer.<sup>15</sup>

17 If, during a dissolution proceeding, one party modifies an instrument making a  
18 nonprobate transfer of community property without the consent of the party’s  
19 spouse, the spouse’s share of the property may be transferred contrary to the  
20 spouse’s wishes. For example, suppose that a husband, with his wife’s consent,  
21 deposits community funds in a P.O.D. account, naming their children as  
22 beneficiaries. Later, during a proceeding to dissolve their marriage, the husband  
23 changes the account to name his brother as beneficiary, without his wife’s consent.  
24 The husband then dies and his brother withdraws all of the funds, including the  
25 wife’s share of the community property.<sup>16</sup> This is exactly the sort of dissipation of  
26 marital assets that the ATRO is intended to prevent. Thus, modification of a

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11. See, e.g., *Redke v. Silvertrust*, 6 Cal. 3d 94, 490 P.2d 805, 98 Cal. Rptr. 293 (1971) (enforcing oral agreement to maintain particular testamentary provision).

12. See, e.g., *In re Marriage of Hilke*, 4 Cal. 4th 215, 222, 841 P.2d 891, 895, 14 Cal. Rptr. 2d 371, 375 (1992) (“severance of a joint tenancy — by eliminating the survivorship characteristic of the joint tenancy form of ownership — theoretically affects the expectancy interest of the other joint tenant, but does not involve a diminution of his or her present vested interest”).

13. Life insurance presents a special case and is discussed separately. See *infra* text accompanying notes 19-20.

14. See *supra* note 3.

15. See Prob. Code §§ 5020 (spousal consent required for nonprobate transfer of community property), 6101 (will may only dispose of testator’s half of community property).

16. See Prob. Code §§ 5403 (P.O.D. account paid to P.O.D. payee on proof of death of original payee), 5405 (payment pursuant to Section 5403 discharges financial institution of all claims regardless of whether payment was consistent with beneficial ownership of account).

1 nonprobate transfer, in a manner that will affect the disposition of community  
2 property, should be restrained by the ATRO.<sup>17</sup>

3 Modification of a nonprobate transfer of separate property does not present the  
4 same risk. However, characterization of property as community or separate often  
5 involves a complex legal and factual determination that is probably best left to the  
6 courts. For this reason, the restraint on modification of a nonprobate transfer  
7 should apply to both community and separate property. This is consistent with  
8 existing law, which restrains transactions involving either community or separate  
9 property.<sup>18</sup>

#### 10 **Creation of a Nonprobate Transfer**

11 Creation of a nonprobate transfer can also pose a risk of unauthorized transfer of  
12 community property. For example, one spouse may use community funds to  
13 establish a P.O.D. account, without the consent of the other spouse, naming a third  
14 party as P.O.D. payee. On the account holder's death, the funds, including the  
15 nonconsenting spouse's share, would be paid to the third party. Thus, for the same  
16 reasons that modification of a nonprobate transfer should be restrained, creation of  
17 a nonprobate transfer should also be restrained.

#### 18 **Life Insurance**

19 Under existing law, the ATRO expressly restrains cancellation or modification  
20 of any type of insurance during a dissolution proceeding.<sup>19</sup> This preserves the  
21 status quo in important ways, such as preventing the cancellation of health  
22 insurance coverage of a spouse. It also helps avoid the problem of an unauthorized  
23 transfer of community property to a third party. Finally, it preserves an asset that  
24 the court can use in fashioning a support order — it is fairly common for the court  
25 to order the obligor spouse to maintain life insurance for the benefit of the  
26 supported spouse, to provide support in the event of the obligor's death.<sup>20</sup> The  
27 court's ability to make such an order might be compromised if the policy were  
28 canceled. For all of these reasons, the existing restraint on cancellation or  
29 modification of insurance policies should be maintained.

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17. Modifications that would be restrained as affecting the disposition of property include a change of beneficiary or of a power of appointment. Modifications that would not be restrained include naming a new trustee or successor trustee (so long as the change does not affect the trustee's powers or duties with respect to disposition of trust property).

Note that a rule permitting revocation of a nonprobate transfer, but requiring spousal consent or a court order in order to modify a nonprobate transfer, is consistent with the rule governing a trust containing community property — either spouse can unilaterally revoke such a trust, but the consent of both spouses is required in order to modify it. See Fam. Code § 761.

18. See Fam. Code § 2040(a)(2).

19. See Fam. Code § 2040(a)(3).

20. See Fam. Code § 4360 (support order may include amount sufficient to maintain insurance on life of support obligor, for benefit of supported spouse).

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RECOMMENDATION

The Commission recommends that Family Code Section 2040 be amended to clarify the scope of the ATRO, consistent with the following principles:

- (1) The ATRO should not restrain the creation, modification, or revocation of a will.
- (2) The ATRO should restrain the creation of a nonprobate transfer.
- (3) The ATRO should restrain modification of a nonprobate transfer if the modification will affect the disposition of property.
- (4) The ATRO should not restrain the revocation of a nonprobate transfer (other than life insurance).<sup>21</sup>

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21. See proposed Fam. Code § 2040(c) (“nonprobate transfer” defined).

## PROPOSED LEGISLATION

### **Fam. Code § 2040 (amended). Automatic temporary restraining order**

SECTION 1. Section 2040 of the Family Code is amended to read:

2040. (a) In addition to the contents required by Section 412.20 of the Code of Civil Procedure, the summons shall contain a temporary restraining order:

(1) Restraining both parties from removing the minor child or children of the parties, if any, from the state without the prior written consent of the other party or an order of the court.

(2) Restraining both parties from transferring, encumbering, hypothecating, concealing, or in any way disposing of any property, real or personal, whether community, quasi-community, or separate, without the written consent of the other party or an order of the court, except in the usual course of business or for the necessities of life and requiring each party to notify the other party of any proposed extraordinary expenditures at least five business days before incurring those expenditures and to account to the court for all extraordinary expenditures made after service of the summons on that party.

Notwithstanding the foregoing, nothing in the restraining order shall preclude a party from using community property, quasi-community property, or the party's own separate property to pay reasonable attorney's fees and costs in order to retain legal counsel in the proceeding. A party who uses community property or quasi-community property to pay his or her attorney's retainer for fees and costs under this provision shall account to the community for the use of the property. A party who uses other property that is subsequently determined to be the separate property of the other party to pay his or her attorney's retainer for fees and costs under this provision shall account to the other party for the use of the property.

(3) Restraining both parties from cashing, borrowing against, canceling, transferring, disposing of, or changing the beneficiaries of any insurance or other coverage, including life, health, automobile, and disability held for the benefit of the parties and their child or children for whom support may be ordered.

(4) Restraining both parties from creating a nonprobate transfer or modifying a nonprobate transfer in a manner that affects the disposition of property subject to the transfer, without the written consent of the other party or an order of the court.

(b) Nothing in this section restrains revocation of a nonprobate transfer, elimination of a right of survivorship between owners of jointly-owned property, or the creation, modification, or revocation of a will.

(c) In all actions filed on and after January 1, 1995, the summons shall contain the following notice:

“WARNING: California law provides that, for purposes of division of property upon dissolution of marriage or legal separation, property acquired by the parties during marriage in joint form is presumed to be community property. If either party to this action should die before the jointly held

community property is divided, the language of how title is held in the deed (i.e., joint tenancy, tenants in common, or community property) will be controlling and not the community property presumption. You should consult your attorney if you want the community property presumption to be written into the recorded title to the property.”

(d) For the purposes of this section:

(1) “Nonprobate transfer” means an instrument, other than a will, that makes a transfer of property on death, including a revocable trust, pay-on-death account in a financial institution, Totten trust, transfer-on-death registration of personal property, or other instrument of a type described in Section 5000 of the Probate Code.

(2) “Nonprobate transfer” does not include a provision for the transfer of property on death in an insurance policy or other coverage held for the benefit of the parties and their child or children for whom support may be ordered, to the extent that the provision is subject to paragraph (3) of subdivision (a).

**Comment.** Section 2040 is amended to clarify the scope of the automatic temporary restraining order with respect to estate planning changes.

Subdivision (a)(4) restrains modification of a nonprobate transfer “in a manner that affects the disposition of property subject to the transfer.” Modifications that are restrained as affecting the disposition of property include a change of beneficiary or power of appointment. Modifications that are not restrained include naming a new trustee or successor trustee (so long as the change does not affect the trustee’s powers or duties with respect to disposition of trust property).

Subdivision (b) provides that the restraining order does not restrain elimination of a right of survivorship between owners of jointly owned property. This codifies *Estate of Mitchell*, 76 Cal. App. 4th 1378, 91 Cal. Rptr. 2d 192 (1999) (restraining order does not restrain severance of joint tenancy). The fact that the restraining order does not restrain revocation of a nonprobate transfer does not mean that such a transfer is necessarily subject to revocation by one party without the consent of the other party. The question of whether a nonprobate transfer is subject to unilateral revocation is governed by the terms of the nonprobate transfer and applicable substantive law. See, e.g., Prob. Code § 5506 (action by all surviving joint owners required to cancel beneficiary registration of jointly-owned security); 31 C.F.R. § 353.51 (restricting changes in ownership of jointly-owned Series EE savings bond).