

## Second Supplement to Memorandum 2000-51

### **Estate Planning During Dissolution of Marriage: Comments of Beverly Hills Bar Association**

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We have received a letter from the Probate, Trust and Estate Planning Legislative Committee of the Beverly Hills Bar Association (“the Committee”) regarding the Commission’s tentative recommendation on *Estate Planning During Marital Dissolution*. The letter is attached.

In general, the Committee agrees with the proposed law. However, it raises several issues, which are discussed below:

#### **Disadvantage to Respondent**

The automatic temporary restraining order (ATRO) in effect during a proceeding for dissolution of marriage takes effect on service of the summons. This means that a petitioner can make estate planning changes *before* service of the summons and thereby avoid the effect of the ATRO. A respondent who is surprised by service cannot. The Committee believes that this is a problem, but does not offer any specific suggestion for how the problem might be solved.

The Commission previously considered whether the potential unfairness to the respondent could be minimized by some sort of retroactive limitation on the petitioner’s actions (e.g., voiding actions of the types restrained by the ATRO that were taken during some fixed period before service of the summons). Retroactive limitation would be analogous to the rule in bankruptcy that allows a trustee to void transfers from a debtor to the debtor’s creditors that occurred within 90 days of filing of the petition. See 11 U.S.C. § 547(b). The Commission rejected the idea of retroactive limitation as creating too many problems. **The staff sees no simple solution to the problem of unfairness to a surprised respondent.**

#### **Proposed Exemptions from Scope of ATRO**

The Committee lists a number of transactions that it believes should not be restrained by the ATRO. These are discussed below:

### *Changing the Beneficiary of a Living Trust*

The Committee suggests that the ATRO should not restrain a change in beneficiary of a living trust. However, one of the principles underlying the proposed law is that the ATRO should restrain estate planning changes that could potentially result in an unauthorized transfer of community property. A change of beneficiary of a living trust has such potential. If one spouse changes the beneficiary of a trust containing community property and then dies, the property may be transferred to the new beneficiary without the surviving spouse's consent. **The staff recommends against the suggested change.**

### *Designating Personal Representative as Beneficiary*

The Committee suggests that the ATRO should not restrain changing the beneficiary of a nonprobate transfer to the personal representative of the party's estate. The risk of such a change resulting in an unauthorized transfer of community property would be small, because the property would be subject to probate administration. In the process of administration the character of the property could be determined and the transfer could be set aside to the extent that it affects the other spouse's community property. However, a party could achieve much the same result simply by revoking the nonprobate transfer (revocation would not be restrained under the proposed law). On revocation of the nonprobate transfer, the party's share of the property would be part of the party's estate, subject to disposition by will. **The staff recommends against the suggested change.**

### *Designating Trustee as Beneficiary*

The Committee suggests that the ATRO should not restrain changing the beneficiary of a nonprobate transfer to the trustee of the party's living trust. However, such a change could potentially result in an unauthorized transfer of community property. For example, suppose that Husband and Wife agree that Wife will establish a pay-on-death account, funded with community property, naming Husband's child from a former marriage as beneficiary. At that time Wife also creates a living trust, funded with her separate property, naming her sister as beneficiary. During a subsequent dissolution proceeding, Wife changes the beneficiary of the POD account to be the trustee of her living trust. On wife's death, the POD account is paid to the trustee who then conveys the property, according to the terms of the trust, to Wife's sister. **The staff recommends against the suggested change.**

*Revocation or Cancellation of Community Property Agreement*

Under existing law, spouses may agree to divide community property on death asset-by-asset, rather than sharing ownership of each asset equally. Prob. Code § 100(b). The Committee points out that such an agreement can be used to minimize taxes by allocating taxable assets to the estate of the surviving spouse. Such an arrangement may not make sense in the context of dissolution. The Committee believes that revocation or cancellation of such an agreement should not be restrained by the ATRO.

The Committee makes a good point. So long as the community property agreement is revocable by either party unilaterally, revocation would not seem to harm either spouse. The planned division of assets would fail (as the parties anticipated that it might, given the agreement's revocability), but the parties present ownership rights and overall shares of community property on death would not be affected. For this reason, **the staff agrees that the ATRO should not restrain revocation of such an agreement.**

It may be that no change to the proposed law is required in order to implement the Committee's suggestion. Under the proposed law, the ATRO does not restrain revocation of a "nonprobate transfer", which it defines as follows:

"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."

An agreement specifying how community property assets are to be divided on the death of a spouse could be understood as an instrument making a transfer of property on death, i.e., a nonprobate transfer. The fact that Probate Code Section 5000 includes a "marital property agreement" in its list of instruments that can constitute a nonprobate transfer supports this interpretation. The fact that a community property agreement should be treated as a nonprobate transfer should probably be clarified by adding the language to the Comment, along the following lines:

**Comment.** ...Subdivision (d) defines "nonprobate transfer" for the purposes of this section. The definition expressly incorporates instruments described in Probate Code Section 5000, including a "marital property agreement." Thus, an agreement between spouses as to how to divide community property between them on either of their deaths is a nonprobate transfer for the purposes of this section.

See Prob. Code § 100(b) (agreement as to division of community property on death of spouse).

*Modification of a Power of Appointment*

The Committee suggests that the ATRO should not restrain modification of a power of appointment. However, modification of a power of appointment could easily result in an unauthorized transfer of community property. For example, before a dissolution proceeding is anticipated, Husband creates a power of appointment in a trust funded with community property (with Wife's consent). After commencement of the dissolution proceeding, Husband modifies the power of appointment, changing the donee to a person more likely to distribute property to his preferred heirs and enlarging the scope of community property subject to the power. This change would directly affect the disposition of Wife's share of the community property. **The staff recommends against the suggested change.**

*Execution of a Disclaimer.*

The Committee suggests that the ATRO should not restrain execution of a disclaimer. Pursuant to Probate Code Section 260 *et seq.*, a person may disclaim an interest in property which he or she would otherwise receive as beneficiary of a will or nonprobate transfer.

One of the principles of the proposed law is that a person should be free to make an estate planning change during dissolution of marriage, so long as the change does not affect the rights of the other spouse. The staff can see no way in which a disclaimer by one spouse would harm the other spouse's interests. For that reason, **the staff agrees that the ATRO should not restrain execution of a disclaimer.** At the risk of making the ATRO even harder to understand by pro se litigants, we could add the suggested exemption by amending proposed Family Code Section 2040(b) as follows:

2040. ...(b) Notwithstanding subdivision (a), nothing in this section restrains any of the following:

...

(6) Execution and filing of a disclaimer pursuant to Part 8 (commencing with Section 260) of Division 2 of the Probate Code .

Respectfully submitted,

Brian Hebert  
Staff Counsel

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Law Revision Commission  
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July 7, 2000

Reply To:

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

Re: Estate Planning during Marital  
Dissolution February, 2000

Gentlemen:

We have reviewed the proposal of the Law Revision Commission regarding estate planning during the marital dissolution. In general we agree with the approach of the Law Revision Commission but believe that the approach falls short in one respect. As pointed out in the preamble to the recommendation, it is clear that the non-petitioning, respondent spouse, is at a disadvantage. We believe that neither spouse should be forced to go to court to accomplish the following changes to his or her estate plan:

- A. Changing the beneficiary designation of a living trust.
- B. Changing the beneficiary on any non-probate transfer to the personal representative of the party's estate or the trustees of the party's living trust.
- C. Revoking or canceling a community property agreement. Community property can now be treated in the aggregate. We are frequently seeing community property agreements that allocate assets between two community halves rather than splitting each asset down the middle. The "creative planning" in some of these agreements consists of allocating the taxable assets, i.e. retirement plans, to the estate of the surviving spouse, thereby allowing optimal funding of the by-pass trust. This can be detrimental to the interest of the surviving spouse.

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D. Modification of a power of appointment or execution of a disclaimer.

These actions can be undertaken without any fear that the Family Law court would lose jurisdiction. We believe they are consistent with the Law Revision Commission's existing recommendation and would generally have the same result. Assets would not automatically be removed from the party's estate, nor from the court's jurisdiction, but would still be subject to the party's disposition at death. Further, there is no reason why a disposition should not be allowed to take place by a trust instead of a will.

Respectfully submitted,

BEVERLY HILLS BAR ASSOCIATION  
Probate, Trust and Estate  
Planning Legislative Committee

By: 

Kenneth G. Petrulis, Chair

KGP/ct

cc: Marc Sallus  
Gary Edelstone