

STATE OF CALIFORNIA

# CALIFORNIA LAW REVISION COMMISSION

RECOMMENDATION

## Estate Planning During Marital Dissolution

October 2000

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

NOTE

This report includes an explanatory Comment to each section of the recommended legislation. The Comments are written as if the legislation were already operative, since their primary purpose is to explain the law as it will exist to those who will have occasion to use it after it is operative.

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CALIFORNIA LAW REVISION COMMISSION

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October 5, 2000

To: The Honorable Gray Davis  
*Governor of California*, and  
The Legislature of California

Existing law imposes an automatic temporary restraining order (“ATRO”) on both parties in a proceeding for dissolution or annulment of marriage, or legal separation. Except as necessary to pay attorney’s fees or ordinary expenses, the order restrains either party from transferring or in any way disposing of any property without the written consent of the other party or an order of the court. The extent to which the restraining order affects estate planning changes that only affect the disposition of property on death is not clear.

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

- (1) The ATRO should not restrain changes that cannot dispose of the other spouse’s property. These include the following:
  - Creation, modification, or revocation of a will.
  - Revocation of a nonprobate transfer.
  - Creation of an unfunded trust.
  - Execution of a disclaimer.
- (2) The ATRO should restrain changes that could dispose of the other spouse’s property. These include the following:
  - The creation of a nonprobate transfer (other than an unfunded trust).

- Modification of a nonprobate transfer if the modification will affect the disposition of property.

This recommendation is submitted pursuant to Resolution Chapter 81 of the Statutes of 1999.

Respectfully submitted,

David Huebner  
*Chairperson*

## ESTATE PLANNING DURING MARITAL DISSOLUTION

Existing law imposes an automatic temporary restraining order (ATRO) on both parties in a proceeding for dissolution or annulment of marriage, or legal separation (hereinafter “dissolution”). Except as necessary to pay attorney’s fees or ordinary expenses, the ATRO restrains the 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.”<sup>1</sup> The extent to which the ATRO restrains estate planning changes during a dissolution proceeding is not clear. The Commission has been informed that different trial courts interpret the ATRO differently — some interpret the ATRO as restraining estate planning changes while others do not.<sup>2</sup>

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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 (D. Kan. 1990) (change of life insurance beneficiary was disposition of property in violation of restraining order). See generally Chapus, *Annotation, Divorce and Separation: Effect of Court Order Prohibiting Sale or Transfer of*

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

## PROBLEMS WITH EXISTING LAW

### Uncertainty

Uncertainty as to whether the ATRO restrains estate planning changes can create a trap for unwary parties and inexperienced practitioners. For example, if a party makes an estate planning change during a dissolution proceeding without first obtaining spousal consent or the permission of the court, and the court interprets the ATRO as restraining such a change, the change may be ineffective and the party may be held in contempt.<sup>4</sup>

### Unintended Transfers

A change in a person's life as significant as dissolution of marriage will often lead to changes in that person's testamentary intentions. If the ATRO prevents a person from making an intended estate planning change and the person dies during the dissolution proceeding, the person's estate will pass in an unintended way. For example, suppose a husband and wife

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*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).

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).

convey their community property into a trust that names the survivor of them as beneficiary and is unilaterally revocable by either. The wife later files for dissolution of marriage and decides to revoke the trust and execute a will devising her share of the community property to her children. Before she can obtain a court order permitting the estate planning changes, she dies, and contrary to her wishes, her husband receives the entire property.

### **Inefficiency**

It appears that a principal purpose of the ATRO provision is to conserve judicial resources by making automatic those types of restraints that are commonly sought and granted in dissolution proceedings.<sup>5</sup> However, if parties to a dissolution routinely wish to make estate planning changes during the proceeding, then judicial efficiency is not served by an automatic restraint of such changes. In fact, estate planning changes during dissolution of marriage appear to be commonplace. In one appellate decision, the court suggests that family law attorneys risk malpractice liability if they do not advise their clients of the need to make estate planning changes during a dissolution proceeding in order to avoid an

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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.

unintended transfer if the client dies during the proceeding.<sup>6</sup> Similar advice is provided in standard family law practice treatises.<sup>7</sup> Considering that careful attorneys will seek spousal consent or an order of the court before taking such actions, the court will be required to hear numerous requests that would be granted in many cases — an apparent waste of judicial resources.

### **Disproportionate Effect on Respondent Spouse**

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

## PROPER SCOPE OF RESTRAINING ORDER

As a general matter, it is inequitable and inefficient to require that a party to a dissolution proceeding obtain spousal consent or an order of the court before making estate planning changes that do not affect the rights of the other spouse. Such a restraint also exceeds the proper purpose of the ATRO —

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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 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).



protecting marital assets from dissipation or concealment. As stated in an Arizona case interpreting a similar provision:

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

Whether different types of estate planning changes could "dissipate the property of the marital estate or place it beyond the court's adjudicatory power" is discussed below.

#### **Transaction Involving a Will**

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

Of course, spouses may agree by contract to make a particular testamentary disposition by will. In such a case, the contract itself serves to restrain modification or revocation of the agreed-upon will provision.<sup>11</sup> It is not necessary that all estate planning changes involving wills be automatically restrained during dissolution proceedings in order to protect these contractual agreements.

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

10. See *supra* note 3.

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).

### Revocation of Nonprobate Transfer

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

### Modification of Nonprobate Transfer

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

If, during a dissolution proceeding, one party modifies an instrument making a nonprobate transfer of community property without the consent of the party’s spouse, the spouse’s share of the property may be transferred contrary to the spouse’s wishes. For example, suppose that a husband, with his wife’s consent, deposits community funds in a

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12. See, e.g., *In re Marriage of Hilke*, 4 Cal. 4th 215, 222, 841 P.2d 891, 896, 14 Cal. Rptr. 2d 371, 376 (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 20-21.

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).

P.O.D. account, naming their children as beneficiaries. Later, during a proceeding to dissolve their marriage, the husband changes the account to name his brother as beneficiary, without his wife's consent. The husband then dies and his brother withdraws all of the funds, including the wife's share of the community property.<sup>16</sup> This is exactly the sort of dissipation of marital assets that the ATRO is intended to prevent. Thus, modification of a nonprobate transfer, in a manner that will affect the disposition of community property, should be restrained by the ATRO.<sup>17</sup>

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

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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).

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).

### **Creation of Nonprobate Transfer**

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

However, there should be an exception for creation of an unfunded trust.<sup>19</sup> So long as no property is transferred to the trust, mere creation of a trust does not pose any risk of unauthorized disposition of community property. Creation of an unfunded trust during marital dissolution would allow a party to establish a detailed instrument to eventually replace any estate planning instrument that is revoked. The unfunded trust could be funded by property that is released from restraint or by a pour-over provision in a will. Allowing creation of an unfunded trust, without spousal consent or an order of the court, also preserves the confidentiality of the terms of the trust.

### **Life Insurance**

Under existing law, the ATRO expressly restrains cancellation or modification of any type of insurance during a dissolution proceeding.<sup>20</sup> This preserves the status quo in important ways, such as preventing the cancellation of health insurance coverage of a spouse. It also helps avoid the problem of an unauthorized transfer of community property to a third party. Finally, it preserves an asset that the court can use in fashioning a support order — it is fairly common for the court to

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19. See proposed Fam. Code § 2040(b)(4) *infra*.

20. See Fam. Code § 2040(a)(3).

order the obligor spouse to maintain life insurance for the benefit of the supported spouse, to provide support in the event of the obligor's death.<sup>21</sup> The court's ability to make such an order might be compromised if the policy were canceled. For all of these reasons, the existing restraint on cancellation or modification of insurance policies should be maintained.

### **Disclaimer**

Under existing law, a person may disclaim an interest in property received pursuant to a testamentary or inter vivos instrument or by operation of law.<sup>22</sup> Such a disclaimer could be considered a disposition of property, subject to restraint under the ATRO. Because property subject to a disclaimer would otherwise be the disclaimant's separate property,<sup>23</sup> there is no risk that a disclaimer will dispose of the other spouse's property. Under the proposed law, execution of a disclaimer is not restrained.<sup>24</sup>

## RECOMMENDED REVISIONS

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 changes that cannot dispose of the other spouse's property. These include the following:
  - Creation, modification, or revocation of a will.

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

22. See Prob. Code § 260-295.

23. See Fam. Code § 770(a)(2) (separate property includes "all property acquired by the person after marriage by gift, bequest, devise, or descent).

24. See proposed Fam. Code § 2040(a)(5) *infra*.

- Revocation of a nonprobate transfer (other than life insurance).<sup>25</sup>
  - Creation of an unfunded trust.
  - Execution of a disclaimer.
- (2) The ATRO should restrain changes that could dispose of the other spouse's property. These include the following:
- The creation of a nonprobate transfer (other than an unfunded trust).
  - Modification of a nonprobate transfer if the modification will affect the disposition of property.

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25. See proposed Fam. Code § 2040(d) (definition of "nonprobate transfer" excludes insurance) *infra*.

## 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 any of the following:*

*(1) Creation, modification, or revocation of a will.*

*(2) Revocation of a nonprobate transfer, including a revocable trust.*

*(3) Elimination of a right of survivorship.*

*(4) Creation of an unfunded trust.*

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

(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 and a donor’s modification of the terms of a power of appointment (this would not include exercise of a power of appointment by a donee). 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)(2) provides that the restraining order does not restrain revocation of a nonprobate transfer. This does not mean that a nonprobate 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 (2000) (restricting changes in ownership of jointly-owned Series EE savings bond).

Subdivision (b)(3) provides that the restraining order does not restrain elimination of a right of survivorship. 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).

Subdivision (b)(4) provides that the restraining order does not restrain creation of one or more revocable or irrevocable unfunded trusts. However, the transfer of property to fund a trust would be restrained under subdivision (a)(2). An unfunded trust created during a dissolution proceeding could serve as a receptacle for property subject to a pour-over provision in a will. Such a trust could also be funded by property that has been released from restraint by the restraining order.

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).

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