

LAW OFFICES

MARSHALL S. ZOLLA

A PROFESSIONAL CORPORATION
2029 CENTURY PARK EAST
SUITE 1020

LOS ANGELES, CALIFORNIA 90067-2911

TELEPHONE (310) 407-0770

FACSIMILE (310) 407-0776

MARSHALL S. ZOLLA*†‡
DEBORAH ELIZABETH ZOLLA
VIVIAN CARRASCO HOSP

*CERTIFIED SPECIALIST - FAMILY LAW
THE STATE BAR OF CALIFORNIA
BOARD OF LEGAL SPECIALIZATION

†A PROFESSIONAL CORPORATION

‡ FELLOW, AMERICAN ACADEMY OF
MATRIMONIAL LAWYERS
WWW.ZOLLALAW.COM

OF COUNSEL

JOEL P. SCHIFF*†
KEHR, SCHIFF & CRANE LLP

*CERTIFIED SPECIALIST - APPELLATE LAW
THE STATE BAR OF CALIFORNIA
BOARD OF LEGAL SPECIALIZATION

†ALSO ADMITTED IN THE STATE OF NEW YORK

**THE INTERDISCIPLINARY NATURE OF
SUBSTANTIVE FAMILY LAW ISSUES**

Marshall S. Zolla, Esq.

Certified Specialist - Family Law
The State Bar of California Board of Legal Specialization

Presented To:
U.S. TRUST
BANK OF AMERICA PRIVATE WEALTH MANAGEMENT
CENTURY CITY
JULY 31, 2018

TABLE OF CONTENTS

	<u>Page</u>
I. <u>PRENUPTIAL AGREEMENTS</u>	1
II. <u>POSTNUPTIAL AGREEMENTS</u>	7
III. <u>TRANSMUTATION AGREEMENTS</u>	9
IV. <u>SPOUSAL FIDUCIARY DUTIES</u>	12
V. <u>ENTERTAINMENT/BUSINESS VALUATION AND GOODWILL</u>	14
VI. <u>AUTOMATIC TEMPORARY RESTRAINING ORDERS</u>	16
VII. <u>FAMILY GIFTS OR ADVANCE OF INHERITANCE RE CALCULATION OF SUPPORT</u>	18
VIII. <u>RETIREMENT PLAN BENEFITS</u>	19
IX. <u>ALTERNATIVE DISPUTE RESOLUTION–MEDIATION CONFIDENTIALITY</u> ...	20
X. <u>CAPACITY TO ENTER INTO BINDING AGREEMENTS</u>	21
XI. <u>ESTATE PLANING CONSIDERATIONS</u>	24

ATTACHMENTS

1. Marshall S. Zolla *Curriculum Vitae*
2. “*Marital Duty*” article reprint published in Los Angeles Lawyer, February 2004
3. “*The California Lawyer’s Grey Fog of Uncertainty: Assessing a Client’s Diminished Mental Capacity*,” Updated and Reprinted, California Family Law Monthly, November 2014
4. “*Mediation Confidentiality vs. Breach of Spousal Fiduciary Duty: The Clash of Enshrined Public Policy Titans*” article reprint published in California Family Law Monthly, July 2012

**Prenuptial
Agreements**

PRENUPTIAL AGREEMENTS

A. INTRODUCTION

Prenuptial Agreements involve rights and obligations of the parties to be considered upon separation/divorce and death, disclosure requirements mandated by California law, estate planning considerations, and an awareness of the emotional sensitivities of the parties approaching and anticipating their marriage. This summary of issues and concerns is not intended to be a comprehensive review and analysis of all issues and provisions in a Prenuptial Agreement.

As an introductory comment to put this matter into proper context, it should be noted that a Prenuptial Agreement is customarily considered to be advisable where there exists some type of imbalance between the two parties contemplating marriage, i.e., an imbalance of wealth, age, business acumen and sophistication, a second marriage, children from prior relationships, cultural differences, lifestyle differences, etc. These factors necessarily impact the decisions made and address and resolve the major issues inherent in this type of agreement.

The timing of when these agreements are finalized and signed is often overlooked, but critically important. We customarily advise that Prenuptial Agreements be signed before save the date and wedding invitations are mailed. Having agreements signed in close proximity to a wedding date is not advisable because it could taint the voluntary nature of the agreement. There is no longer a seven day waiting period between the date a draft is first given to a party against whom enforcement is sought and when it is signed as set forth in Family Code section 1615(c)(2) if both parties are represented by independent counsel from the beginning of negotiations of the Prenuptial Agreement. (*In re Marriage of Cadwell-Faso & Faso* (2011) 191 Cal.App.4th 945.) It is important to be mindful that Prenuptial Agreements are customized and tailored agreements that require full disclosure of both parties' respective assets and debts, as explained in greater detail below. It is for this reason that prudent practice requires starting the negotiation and drafting of a Prenuptial Agreement months in advance of a wedding date so there is sufficient time to properly negotiate and draft the agreement.

B. POST-MARITAL EARNINGS AND INCOME OF THE PARTIES

Generally speaking, earnings of the parties from their personal services after marriage are considered community property. For parties with significant earnings and income, a Prenuptial Agreement can alter this provision of California law, and provide that any and all post-marital earnings and income of the parties be deemed and considered separate property. This may be particularly important where the total compensation of a party includes a variety of factors, such as earned income, passive dividends, interest income, partnership distributions, stock options, royalties, residuals, etc.

C. CHARACTERIZATION OF PROPERTY

The main purpose of a Prenuptial Agreement is to set forth in detail the assets and obligations that each party brings to the marriage. A detailed list of the assets and obligations of each party is set forth on the exhibits to the agreement. The agreement then provides that the assets and obligations that each person owns at the date of marriage are confirmed to that person as their sole and separate property.

It is both possible and likely that the assets that each party brings to the marriage will appreciate over time. For example, if one party owns an asset worth \$1,000,000 at the date of marriage, it is possible that such asset could appreciate in value over time. In the event the parties later separate or divorce, the question could arise whether the community property of the parties has an interest in the appreciation of that asset. A well drafted Prenuptial Agreement can make certain that any appreciation of the asset owned by a party at the time of marriage remains the sole and separate property of that person, whether the appreciation is due to passive returns, the active involvement of the party, mixed efforts, market forces, or otherwise. Protecting such appreciation is an essential ingredient of a properly drafted Prenuptial Agreement.

In many instances, one party will own a residence (or several residences) at the time of marriage. The parties may decide to live in that residence and have an existing mortgage paid with post-marital income, thereby providing the community estate with an interest in what should be a separate property residence. A properly drafted and constructed Prenuptial Agreement can eliminate that possibility, if the separate property residence of one of the parties is kept as that party's sole and separate property because it is paid with their income which under the terms of the agreement is separate property. If the respective parties' income is not characterized as separate property by virtue of the agreement, the party who owns the home can maintain its separate property nature by paying any existing mortgage from separate property funds brought to the marriage. In the event a separate property home is transmuted from one party's separate property to community property, the party without the wealth must be advised that that does not mean they own the home equally because the party who owned the home prior to such transmutation likely has a reimbursement claim under Family Code section 2640 for separate property contributions to the down payment, mortgage, and improvements. The present and future living situation of the parties must also be carefully discussed and considered (e.g., what happens to the residence(s) upon either party's death or upon separation/divorce). We work closely with experienced estate planning counsel to ensure that such provisions in a Prenuptial Agreement are consistent with the provisions of the client's estate plan.

D. JOINT LIVING EXPENSES

If the Prenuptial Agreement changes the community property rules to provide that post-marital earnings and income remain separate property, the parties must decide how and in what manner they wish to fund their ongoing joint living expenses, and that can also be set forth in the Prenuptial Agreement, with as much flexibility or detailed precision as the parties may desire. The parties should also specify which party will pay for medical and dental insurance.

E. MUTUAL SPOUSAL SUPPORT WAIVER OR LIMITATION

It is now permissible under California law for parties to provide that in the event of a separation or divorce, each party waives the right to claim or receive spousal support. Family Code section 1612(c) contains the statutory provisions and conditions of an effective spousal support waiver. In addition to a waiver of potential future spousal support, parties are also permitted to contract to limit future spousal support.

It is important to point out that the party against whom enforcement is sought must be represented by independent counsel if there is a waiver of support. It is further important to point out that the effectiveness of a spousal support waiver is tested not at the time of execution of the Prenuptial Agreement [as would be the case with other provisions of a contract], but enforceability is tested based upon unconscionability “at the time of enforcement.” This is a relatively new concept from the much debated decision of *In re Marriage of Facter* (2013) 212 Cal.App.4th 967. Because of the holding in the *Facter* case, as explained below, any Prenuptial Agreement with a mutual spousal support waiver must distinguish its facts from the facts in *Facter* and should contain a limitation of support provision in the agreement in the event the spousal support waiver is deemed to be unconscionable at the time of enforcement. Prudent practice also requires that counsel representing the party who wants the spousal support waiver write a letter to their client explaining the uncertainty of whether the spousal support waiver will be enforced at the time of enforcement in light of the *Facter* case.

In *In re Marriage of Facter, supra*, 212 Cal.App.4th 967, the Court of Appeal held that the test of whether or not a spousal support waiver is unconscionable is determined at the time of enforcement, not at the time a Prenuptial Agreement is executed. The facts of *Facter* are instructive. At the time the Prenuptial Agreement was signed, Nancy was a recently unemployed high school graduate with two minor children, living rent free in the home of her fiancé, Jeffrey, who was an accomplished attorney who earned \$500,000 per year and had \$3 million dollars of separate property. Jeffrey drafted the agreement and advised Nancy that the spousal support waiver could not be negotiated. Nancy took the agreement to two different attorneys to review, but did not retain an attorney or have an attorney sign the Agreement. She was advised by those attorneys that the provisions related to child support and attorney fees were unenforceable and that there was no waiver of spousal support. She was also advised that Jeffrey’s earnings would become community property if they were deposited into a joint bank account. At the time of enforceability, Nancy received \$200,000 because the parties were married longer than 15 years, one-half the equity in the home after reimbursements to Jeffrey for his down payment and costs of sale, and a Jaguar. The Court of Appeal found that Nancy did not work during the parties’ 16 year marriage or pursue her education, but focused on raising the parties’ child and maintaining the family home. The Court of Appeal based its holding that the agreement was unconscionable at the time of enforcement upon its finding that Nancy could not have come close to replicating the family standard of living. Jeffrey had separate property in excess of \$10 million and earned \$1 million per year and Nancy had neither separate property nor income. This is an important case from 2013, has engendered considerable debate, and should be carefully explained to the parties incident to the negotiation of a Prenuptial Agreement.

F. ANNUAL PAYMENTS

When a spousal support waiver is included in the agreement, counsel sometimes include annual payments on the anniversary of the parties' marriage for a certain period of time, either to the spouse without the wealth, or to the community, so the agreement provides mutual advantages. If other advantages are provided in the Agreement to the spouse without the wealth both upon death or divorce, such as receiving spousal support, an interest in a home, or an interest in a pension plan or IRA, then annual payment provisions may not be appropriate. The rationale for including an annual payment provision is so the spouse without wealth does not walk away from the marriage with nothing upon the other spouse's death or divorce. *In re Marriage of Burkle* (2006) 139 Cal.App.4th 712 discusses the importance of Prenuptial Agreements containing mutual advantages for them to be valid and enforceable agreements.

G. MUTUAL WAIVERS OF RETIREMENT PLAN BENEFITS

It is often customary to include waivers of spousal benefits for both parties' retirement plans and IRAs which they would otherwise be entitled to as a result of their marriage. Many retirement plans have a waiting period for spouses to execute such waiver forms, so we provide that both parties will sign when they are legally able to do so. We have experienced pension experts draft retirement provisions. We then instruct the estate planning attorney or business manager to ensure that the clients execute these forms in a timely manner.

H. LIFE INSURANCE

Life insurance provisions are customarily included in Agreements if the party without the wealth does not inherit the family home after the other party's death. Such insurance policy or trust is usually established within a specified period of time after the parties' marriage and remains in effect for a limited amount of years or until either party files a Petition for Legal Separation or Dissolution of Marriage.

I. ESTATE PLANNING

A Prenuptial Agreement is not a testamentary instrument. It is crucially important, therefore, that the provisions of a Prenuptial Agreement be carefully reviewed by experienced estate planning counsel, to make certain that the provisions of the Prenuptial Agreement are in harmony with the testamentary intent and estate planning documents of the party.

J. GOVERNING LAW

Family Code section 1612(a)(6) provides: "The choice of law governing the construction of the agreement" is a permissible provision in a Prenuptial Agreement. Parties with significant assets in the United States and in foreign jurisdictions, who may also maintain residences in different places within the United States, or in the United States and foreign countries, may find it advantageous to specify a choice of law (meaning which state or country's law will govern

their agreement). Our transient society, where individuals and families often relocate and move, is also a factor to consider regarding which law applies to the Agreement. This can be inordinately complicated, and depend upon the contacts of the parties with a particular place, tax considerations, estate planning considerations, etc.

K. MATERIAL PROVISIONS WHICH CANNOT BE INCLUDED IN A PRENUPTIAL AGREEMENT

The issue of child support with respect to a future child of the marriage may not be included in a Prenuptial Agreement. (*Family Code* §1612(b).) Matters of child custody are not properly part of a Prenuptial Agreement. Often times there are religious or cultural differences between parties, and the parties may seek to specify the religious upbringing of a future child of the marriage. In California, such a provision is not valid and enforceable pursuant to *In re Marriage of Weiss* (1996) 42 Cal.App.4th 106 (rev. denied. cert denied (1996)).

L. DISCLOSURE REQUIREMENTS

California Family Code section 1615 sets forth a list of requirements for a Prenuptial Agreement to be valid and enforceable. One of the requirements is that each party is required to make full disclosure of that party's assets, liabilities, and net worth. We work closely with accountants and business managers to accurately reflect parties' assets and debts on their respective exhibits to the Prenuptial Agreement. In many instances, the parties to the contemplated marriage (or in many instances, the family) is reluctant to disclose the nature, extent, valuation, location and composition of all of the party's assets and obligations. Failure to do so is a risk that the agreement will not be found valid and enforceable, if it is ever tested.

The compiling and documentation of the assets and liabilities of a party is customarily one of the most time consuming and difficult elements of preparing a Prenuptial Agreement. In addition, it is often the case, that the party involved and contemplating marriage may not be fully aware of the nature and extent of all interests that party owns, or in which that party may have an interest. That poses a problem which requires attention and resolution in order for the party to fulfill the obligation of full and timely disclosure.

M. CONFIDENTIALITY

Both parties to a Prenuptial Agreement must be represented by independent counsel. Therefore, the disclosures made by each party will be made known not only to the other party, but to the other party's counsel, and perhaps other advisors. It is prudent to include a well-drafted confidentiality provision in the Prenuptial Agreement and, sometimes, a separate Confidentiality Agreement is prepared and executed contemporaneously to safeguard, to the extent possible, the confidentiality of all financial information disclosed and exchanged.

N. MEDIATION

If there is a substantial imbalance in wealth, having a Prenuptial Agreement mediated provides an extra layer of protection because the mediation confidentiality statutes set forth in Evidence Code section 1119 *et seq.* make it virtually impossible to invalidate such an agreement if it is mediated. Mediation confidentiality is so important and enshrined in California law that such confidentiality statutes trump and prevail over fiduciary duty statutes. By way of example, if one party does not disclose a material asset on their Exhibit to the Prenuptial Agreement, mediation confidentiality will prevail over the lack of disclosure and the agreement will be upheld.

Attached as Tab 4 is copy of article entitled: "*Mediation Confidentiality vs. Breach of Spousal Fiduciary Duty: The Clash of Enshrined Public Policy Titans*" featured in the June 2012 issue of the California Family Law Monthly, published by Matthew Bender.

POSTNUPTIAL AGREEMENTS

Postnuptial agreements between spouses, unlike prenuptial agreements between intended spouses, are not governed by statute. Postnuptial agreements are a matter of contract and, since they are executed between spouses, are further governed by the concepts of fiduciary duties between spouses. This means that there is a heightened duty to disclose the parties' respective assets. Postnuptial Agreements are often negotiated and drafted when parties run out of time to prepare a Prenuptial Agreement, amend an earlier Prenuptial Agreement later in their marriage, transmute separate property to community property, are a tax planning device, or when couples are contemplating separation.

The main case which explains and interprets the nature and scope of Postnuptial Agreements, is *In re Marriage of Burkle* (2006) 139 Cal.App.4th 712:

This case engendered significant notoriety. The issue was the enforceability of a post marital agreement. The trial court found the agreement valid and enforceable; that was affirmed by the Court of Appeal. The chief findings of the case were as follows:

A. A presumption of undue influences does not arise in an inter-spousal transaction unless one spouse obtains an *unfair advantage* or obtains property for which no or clearly inadequate consideration has been given. The presumption does not apply to a postnuptial agreement in which both spouses obtain advantages, both are represented by independent and competent legal counsel, the wife is offered full access to the husband's business records relating to the marital assets, and both spouses acknowledge in the agreement that neither has obtained an unfair advantage as a result of the agreement.

B. Even if a presumption of undue influence did apply with respect to the parties; post marital agreement, and even if the trial court erred in allocating to the wife the burden of proving the agreement was invalid, substantial evidence supported the trial court's finding that credible evidence "established overwhelmingly" that the agreement was not procured by undue influence.

C. Wife's claim that the post marital agreement was procured by the husband through actual fraud, by reason of his failure to provide written information to her on the effects of a prospective merger that would later affect the value of marital assets, was found to be without merit.

D. Family Code sections 2104 and 2105, requiring parties to a marital dissolution action to serve formal Preliminary and Final Declarations of Disclosure on Judicial Council forms disclosing all of their respective assets and liabilities, do not apply to spouses who negotiate and execute a post marital agreement while a dissolution proceeding is in abeyance, and the spouses are attempting to reconcile, rather than contemplating the imminent dissolution of their marriage.

E. Wife's claim that she properly rescinded the post marital agreement for "non-performance and failure of consideration" is without merit, because wife repudiated the agreement in her dissolution Petition, excusing further performance by husband pending judicial determination of the validity of the agreement.

F. The doctrines of ratification and estoppel operate to preclude wife from claiming that the post marital agreement was unenforceable.

TRANSMUTATION AGREEMENTS

There have been several transmutation cases in recent years, where parties prior to a separation or divorce, try and change the character of property from separate property to community property or vice versa, as set forth below. No transmutation occurs unless the requirements of Family Code section 852 are met. This is a good example of where estate planning and family law intersect because if parties go to an estate planning attorney to try and change the character of their property, the estate planning attorney may or may not use the correct language to satisfy Family Code section 852 and they often do not advise clients how such transmutation agreements can impact their rights in a divorce proceeding. Estate planning attorneys at that juncture should refer each client to an experienced family law practitioner. Family law attorneys should always be mindful of whether an estate plan transmutes any property, because that may substantially impact an eventual dissolution proceeding.

A. *In re Marriage of Valli* (2014) 58 Cal.4th 1396: This is a decision of the California Supreme Court explaining and clarifying the requirements for transmutation of community property to separate property in California. In Valli, during marriage husband took out a \$3.75 million insurance policy on his life, designating wife as the policy's sole owner and beneficiary. The parties in that case did not dispute that the policy was purchased with community property funds from a joint bank account. What they did dispute was the policy's characterization. Husband contended that the life insurance policy was community property because it was purchased during the marriage with community funds. On the other hand, wife argued that the policy was her separate property because Husband arranged for the policy to be put solely in her name, thereby changing the policy's character from community property to separate property. The Supreme Court sided with the Husband, holding that the insurance policy bought with community assets was community property, and that no transmutation occurred when Husband transferred the policy to Wife's name because there was no express declaration made by the Husband who was the spouse whose interest could have been adversely affected.

B. *In re Marriage of Lafkas* (2015) 237 Cal.App.4th 921: The Court of Appeal held that a husband's separate property interest in a real estate partnership was not transmuted to community property, despite a modification of the partnership agreement during the marriage, signed by the husband, which substituted the names of both parties as husband and wife, to replace the name of husband alone, as owners of a one-third interest in the partnership. The modification of the partnership agreement did not contain an "express declaration" that the character or ownership of the partnership was being changed. The court concluded that the transmutation requirements of Family Code section 852 must be met and satisfied before the joint title presumption of section 2581 applied. This case, which has engendered quite a bit of comment and controversy, is important because it is a common occurrence for a spouse's name to be added to the title of premarital property. The Lafkas opinion is therefore of interest and enlightening to issues concerning community property presumptions, transmutations, or debts.

C. *In re Marriage of Bonvino* (2015) 241 Cal.App.4th 1411: *Bonvino* is the latest "no transmutation" case, holding that if property is acquired during marriage with both separate and

community funds, the transmutation requirements of section 852 must be satisfied before the reimbursement provisions of section 2640 apply. In reaching that conclusion, the extensive *Bonvino* opinion summarizes the parade of past invalid transmutation cases, including *Starkman* (2005), *Barneson* (1999), *Estate of Bibb* (2001), and *In re Marriage of Leni* (2006). Any community property interest in the *Bonvino* family home must be calculated according to the *Moore/Marsden* formula, not a 2640 reimbursement without a valid transmutation, which did not occur here. The *Bonvino* case also contains a historical review of the evolution of transmutation issues, from the 1965 enactment of Evidence Code section 662, the threshold *Lucas* decision of the California Supreme Court in 1980, 1984 Law Revision Commission Recommendations re transmutation protections, and legislative enactment of transmutation requirements in former Civil Code sections 5110.710 through 5110.740 (now Family Code sections 850-853), *Estate of MacDonald* in 1990, and its requirement of requisite language of intent mandated by the Supreme Court, and on to the modern exposition set forth by the Supreme Court in *In re Marriage of Valli* in 2014.

There are three older transmutation cases that deal with both family law and estate planning issues, which are essential to keep in mind, as follows:

1. *In re Marriage of Starkman* (2005) 129 Cal.App.4th 659, where the Court held that language in a revocable trust instrument which provided that the property transferred to the trust was community property *unless* Husband or Wife identified it as separate property was *insufficient* to create a transmutation of Husband's separate property to community property. The estate planning documents and stock brokerage transfer forms did not establish a transmutation.

2. *In re Marriage Holtemann* (2008) 166 Cal.App.4th 1166, went the other way, holding that a Transmutation Agreement *did effect* a valid transmutation of separate property to community property, notwithstanding language that purported to qualify, limit or condition the transfer upon the death of either spouse. Although the documents in the *Holtemann* case were for estate planning purposes, regardless of that motivation, they were held to contain the requisite express, unequivocal declarations of transmutation. For estate planning lawyers, the issue of transmutation of property continues to be a perilous area where they can find themselves dangerously close to committing malpractice by failure to consider the effects of these types of estate planning documents in the family law context. For family law attorneys, the *Holtemann* case illuminates the importance of counsel for the non-owner spouse conducting a proper title search, to ascertain if the subject property has ever been put in a family trust. If it is found that property has been transferred to a family trust, inquiry must be made to the estate planning attorney for the entire file, in order to determine if a community property agreement, spousal property transmutation agreement or other such agreement exists, which will have a material bearing on whether or not a transmutation has occurred.

3. *In re Marriage of Lund* (2009) 174 Cal.App.4th 40, followed the reasoning and conclusion of *Holtemann* in finding a valid transmutation in the estate planning and trust documents there at issue. The Court of Appeal found that the agreement in question was not ambiguous and constituted a valid transmutation. The *Lund* Court, interpreting the subject

agreement as a whole and analyzing it alongside *Holtemann* guidelines, concluded that it unambiguously effected a transmutation of husband's separate property into community property.

As can be seen from the above cited cases, preparation of transmutation agreements is technical and requires careful crafting of the parties' intent. Those professionals advising clients with respect to their property rights, whether in a family law context or in an estate planning context, or otherwise, should be guided by the words and wisdom of that well-known legal philosopher and Yankee catcher, Yogi Berra: "If you don't know where you're going, you might end up somewhere else."

SPOUSAL FIDUCIARY DUTIES

Attached as Tab 2 is copy of an article entitled *Marital Duty*, published in the February 2004 Los Angeles Lawyer Magazine, examining and analyzing the scope of the spousal fiduciary duty between spouses pursuant to Family Code section 721.

Spouses owe each other a fiduciary duty under Family Code section 721 (i.e., a heightened and continuing duty to disclose all assets and debts, to deal fairly with each other, and not to obtain an unfair advantage over the other in interspousal transactions.) A rebuttal presumption of undue influence arises when one party obtains an advantage over the other. When they separate, that fiduciary duty continues under Section 2102. The advantaged party usually bears the burden of rebutting the presumption. “In most instances, when a client walks into the practitioner’s office, he or she is already in breach of his or her fiduciary duty.” [New 4 Volume Publication Complex Issues in California Family Law by Matthew Bender & Co., See Volume A, Chapter A1.02] The fiduciary duty ends when assets are *actually distributed and divided*. [Family Code section 2102; *In re Marriage of Hixson* (2003) 111 Cal.App.4th 1116, 4 Cal.Rptr.3d 483.]

Since the publication of the attached article in 2004, there have been numerous cases interpreting the nature and scope of the fiduciary duty between spouses including the following:

A. *In re Marriage of Schleich* (2017) 8 Cal.App.5th 267: Violations of the duties of disclosure involving separate property, community income expended prior to separation, and loan repayments received pre-separation were not breaches of fiduciary duty because they did not impair any interest in the community estate. The alleged violations of disclosure could not support an award of attorneys’ fees under Family Code section 1101(g), because they did not amount to fiduciary breaches. However, the Court found support for an award of sanctions under Family Code section 2107(c). One way or another, failure to disclose leads to adverse consequences.

B. *In re Marriage of Brandes* (2015) 239 Cal.App.4th 1461: Imbedded in the important and lengthy opinion is a discussion of spousal fiduciary duty. Wife contended that when Husband contributed his community efforts to his separate property business, he breached his fiduciary duty to the community. After a review of applicable case law, the Court of Appeal rejected that argument, holding that there was nothing secretive or self-serving about Husband’s conduct. It was no secret that he devoted his personal efforts to his separate property business during the marriage and Wife agreed to that. The Court observed that it would be “absurd” to claim that Husband’s conduct was detrimental to the community when his business’ extraordinary success allowed the parties to achieve an opulent marital lifestyle and amass a fortune in real estate and other holdings, which greatly benefitted Wife during and after the marriage.

C. *In re Marriage of Woolsey* (2013) 220 Cal.App.4th 881: This was an important case that held the presumption of undue influence between spouses does not apply in Marital

Settlement Agreements reached through private mediation. The Court of Appeal held that parties to a marital dissolution who reach agreement on provisions in a marital settlement agreement by voluntarily participating in private mediation may agree to make financial disclosures that do not strictly comply with the need to exchange Preliminary and Final Declarations of Disclosure in a formal manner pursuant to Family Code sections 2104 and 2105.

D. *In re Marriage of Feldman* (2007) 153 Cal.App.4th 1470: Husband was properly sanctioned for his failure to immediately update disclosures and provide Wife with information regarding his financial dealings during their marital dissolution proceeding; there is no need to wait until the end of litigation to assess Family Code section 271 sanctions.

E. *In re Marriage of Kieturakis* (2006) 138 Cal.App.4th 56: Where a Marital Settlement Agreement is the product of mediation, the public policy favoring mediation confidentiality and finality of judgments prevails over the presumption of undue influence in inter-spousal transactions. The burden of proving undue influence is placed upon the party seeking to set aside a mediated agreement under Family Code section 2122.

F. *In re Marriage of Burkle [Burkle II]* (2006) 139 Cal.App.4th 712: The Court of Appeal held a postnuptial agreement between spouses to be valid and enforceable. The scope of the fiduciary duty between spouses was narrowed from the previous standard of one spouse obtaining “an advantage” to the narrower standard of one spouse having obtained “an *unfair* advantage.”

G. *In re Marriage of Mathews* (2005) 133 Cal.App.4th 624: The burden of proof to overcome the Family Code section 721 presumption of undue influence is a preponderance of the evidence; the presumption was overcome in this case because the evidence showed that Wife understood the purpose of a Quitclaim Deed and was under no pressure to sign it. The lesson learned here is where there is no evidence of undue influence, courts are not going to set aside agreements simply because one spouse benefitted over the other. Case law appears to be developing based on factual differences and courts will continue to take a pragmatic approach to fiduciary duties and simply ask if the disadvantaged spouse understood the transaction and whether any undue influence was brought involved in the transaction.

H. *In re Marriage of Brewer and Federici* (2001) 93 Cal.App.4th 1334: A Marital Settlement Agreement and Judgment were properly set aside because Wife listed “unknown” for the value of her NBC pension and GE stock options when she had not tried to ascertain the value of the NBC pension. Husband claimed he entered into the Marital Settlement Agreement and Judgment based on a unilateral mistake because of her insufficient disclosures. The Marital Settlement Agreement and Judgment were set aside because Husband did not have accurate and complete information or valuations of Wife’s pension plans, which information was essential to his agreement to resolve all financial issues. The Court of Appeal held that lack of full and accurate disclosure may be grounds to set aside a Judgment based upon mistake and that Wife was in a better position to obtain the information to make a proper and adequate disclosure.

ENTERTAINMENT/BUSINESS VALUATION AND GOODWILL

A. *In re Marriage of McTiernan and Dubrow* (2005) 133 Cal.App.4th 1090: An individual performing services as a “natural person,” as opposed to as a business or profession, cannot have goodwill; “celebrity goodwill” not recognized.

B. *In re Marriage of Finby* (2013) 222 Cal.App.4th 977: This case, which has received a great deal of attention from commentators and creative lawyers, may quickly attain iconic status. Is a “book of business” now equated to personal goodwill? Has the distinction between “enterprise goodwill” and personal goodwill been eroded? Despite language to the contrary in the *Finby* opinion, will this be viewed as the “anti-*McTiernan*” case, setting a new standard for producers, stockbrokers, real estate agents, financial professionals...? The list goes on. Will client lists now be subject to discovery? Will client lists have to be valued? How will confidentiality concerns be handled if a “book of business” is crucial to the valuation and goodwill determination?

In an acknowledged case of first impression, the Court of Appeal, reversing the trial court ruling, held that “wife’s status as a licensed financial advisor with the ability to induce clients to follow her when transferring to a new firm is similar to the goodwill found in the business of other professions such as lawyers and doctors.”

The *Finby* Court does a delicate “*McTiernan*” dance. The opinion states that it does not disagree with the *McTiernan* ruling, but distinguishes the factual situation of John McTiernan’s high standing and reputation as a motion picture director (no goodwill), as opposed to Rhonda Finby’s substantial book of business transferred with her to her new firm, for which Wachovia Securities paid a substantial bonus. At this point, it would be wise to reread the concurring and dissenting opinions in *McTiernan*. The fine legal line (actually, not so fine) drawn in the *Finby* opinion is certain to engender much debate and litigation as future factual scenarios are argued, negotiated, and brought to the Courthouse, with considerable evidentiary baggage on both sides. Interestingly, no mention is made in the *Finby* opinion of the *McTiernan* dictate that “the expectation of continued public patronage must be generated by ‘a business.’”

There are now new probing questions to ask when analyzing the issues in a new case. Reread this opinion. Be certain to read the many commentaries that have followed. Now appears to be a good time to recall F.W. Maitland’s well-known legal metaphor: “The law is a seamless web.” (The web just got a lot more complex.)]

C. *In re Marriage of Brandes* (2015) 239 Cal.App.4th 1461: In this 2015 business valuation case, the Court of Appeal determined that when the personal efforts of one spouse increase the value of that spouse’s separate property business, the trial court must determine how much of the increased value should be attributable to community property. It is customary to use two formulas for such determination. The *Pereira Formula* is appropriate where business profits are primarily attributable to community efforts. This formula allocates a fair return to the separate property investment in the business and the balance to its increased value to the community. The

Van Camp Formula is appropriate and applicable where business profits are primarily attributable to factors other than community personal services. This formula allocates the reasonable value of the personal services to the community property, and the balance to separate property. The choice of the formula to use is to be based on which formula will be the more substantially equitable and just, but there are no precise standards for a Court making the choice. In the *Brandes* case, in a case of first impression, the Court used a hybrid *Pereira/Van Camp* method to determine and apportion the community interest in Husband's separate property business. The *Brandes* case is generally viewed as one of the most important family cases issued during 2015. Review of this case was denied by the California Supreme Court on November 24, 2015.

**Automatic Temporary
Restraining Orders**

AUTOMATIC TEMPORARY RESTRAINING ORDERS

A. Considerations and Action to Take Prior to Filing a Petition for Legal Separation or Dissolution of Marriage

1. Change of Life Insurance and Retirement Plan Benefit Beneficiaries
2. Change of Estate Plan and Readjustment of Funding of Trusts
3. Transferring of Funds in Bank Accounts

B. ATROS Become Effective When a Party Files a Petition for Legal Separation Or Dissolution of Marriage or Is Served with a Petition and at That Point Parties Are Restrained from Taking Certain Actions under Family Code Section 2040(a)(2)

1. Gale v. Superior Court - The Demise of the Vanilla Pleading: Another pre-filing consideration is whether you plan on filing a *lis pendens* to cloud the title of a property. This is something that needs to be thought out and considered before filing a Petition or a Response. It is no longer sufficient to put the same routine boilerplate catch-all language in the Petition or Response anymore. If you plan on filing a *lis pendens*, you are now required to specifically plead the property in the Petition or Response (i.e., by listing the address). As we will see later, not doing so can have severe consequences.

2. The Unaddressed Conflict between Family Code Section 2040 and 2010

a. Family Code section 2040 prevents a spouse from transferring separate property, but there exists an unaddressed conflict between Section 2040 and Section 2010, which provides that the Court has no jurisdiction over a spouse's separate property.

b. Recent California case law has reaffirmed the Legislature's intent in enacting Family Code section 2010, explaining that the Court's jurisdiction over a spouse's separate property is strictly limited to determining the character of a spouse's separate property (*In re Marriage of DeGuigne* (2002) 97 Cal.App.4th 1353, 1365; *In re Marriage of Braud* (1996) 45 Cal.App.4th 797, 810; *In re Marriage of Buford* (1984) 155 Cal.App.3d at 78.) The two statutes may be partially harmonized only through an analysis of the legislative history, indicating that section 2040 was for the limited purpose of maintaining temporary status quo and to permit gathering of evidence regarding characterization.

c. Lee v. Superior Court and Family Code Sections 2108 and 2010: A party wishing to sell property should turn to *Lee* and Family Code sections 2108 and 2010. Section 2108 codified the holding in *Lee v. Superior Court* to provide the Court with authority to permit a party to sell community or quasi-community property during a marital dissolution proceeding. The Court in *Lee v. Superior Court* provides that a trial court can with appropriate

safeguards (i.e., any commercially reasonable safeguards to protect a party's alleged interest in the referenced assets due to the other party's restructuring of the assets), require one potential community asset to be sold to save another such asset. The lesson to be learned from *Lee* is that a party can successfully ask the Court to sell one property to save another. To bring a *Lee* or a Section 2108 Motion, the moving party must serve their Preliminary Declaration of Disclosure.

C. How to Enforce the ATROS

1. A party seeking to enforce an ATRO restraint should contend that all property at issue in the divorce may have an alleged community property interest and that Family Code section 1102(a) precludes unilateral selling or encumbering of community real estate.

2. As a result of Family Code sections 2040 and 1102, this position would contend that the other spouse is prohibited from selling, transferring or encumbering real property, regardless of whether a separate interest is alleged to exist.

D. Enforcement by Contempt [Family Code Section 233(c); Penal Code Section 273.6]

1. The ATROS themselves do not prevent a sale or transfer of property. If a party sells or transfers property in violation of the ATROS, a bona fide purchaser acquires good title. The violation may be punished by contempt, by a claim of breach of fiduciary duty or by an adjusted (offset) allocation of community property. Thus, availability of a *Lis Pendens* in compliance with the recent opinion in *Gale v. Superior Court* becomes of more critical importance to assure effective prevention of an improper sale or transfer.

2. Family Code section 233(c) provides, "A willful and knowing violation of any of the other orders included in the summons is punishable as provided in Section 273.6 of the Penal Code."

3. Penal Code section 273.6 provides "Any intentional and knowing violation of a protective order, as defined in Section 6218 of the Family Code, or of an order issued pursuant to Sections 527.6 or 527.8 of the Code of Civil Procedure, or Section 15657.03 of the Welfare and Institutions Code, is a misdemeanor punishable by a fine of not more than one thousand dollars (\$1,000), or by imprisonment in a county jail for not more than one year, or by both that fine and imprisonment."

E. Another Important Overlooked Gap in the Law: ATROS Expire upon Entry of Judgment [Family Code Section 233(a)]; Fiduciary Duties Continues Until Actual Division of All Assets [Family Code Section 2102(a).]

**FAMILY GIFTS OR ADVANCE OF INHERITANCE RE
CALCULATION OF SUPPORT**

A. *In re Marriage of Alter* (2009) 171 Cal.App.4th 718. Family law trial court has discretion to include recurring gifts as income for the calculation of child support; see also, *Kevin Q. v. Lauren W.* (2011) 195 Cal.App.4th 633 which held that gifts to the mother of the minor child were properly considered as income when evaluating the parties' respective ability to pay attorneys' fees in a paternity proceeding.

B. *In re Marriage of Williamson* (2014) 226 Cal.App.4th 1303. The *Williamson* Court distinguished the *Alter* inclusion of recurring gifts as income for the calculation of child support and determined that monies advanced by Husband's wealthy parents were advancements of gifts from the son's inheritance, rather than loans, and that such advances could not be included as income for purposes of calculating Husband's child support obligation. The *Williamson* Court left open the unanswered question of whether transfers from a parent, characterized as either loans or gifts, may be concerned in calculation of spousal support under Family Code section 4320.

C. *Anna M. v. Jeffrey E.* (2017) 7 Cal.App.5th 439. In this 2017 paternity case, the mother of the 10 year old child was cohabiting with a man who considered her to be his closest best-friend; although they had no romantic involvement, he considered the child his god-daughter and paid all bills and expenses for the mother and child. The expenses he paid averaged over \$30,000 per month. The Court of Appeal did not consider the payment of those expenses as the Mother's income and determined that the trial court did not abuse its discretion in failing to consider the recurring payments to Anna as income when calculating child support. The Anna M. Court observed that the *Alter* opinion, which came to a different conclusion, did acknowledge that the question of whether gifts should be considered as income for purposes of a child support calculation is one that should be left to the discretion of the trial court. The Anna M. Court followed the *Williamson* holding in finding no abuse of discretion for the trial court's ruling declining to base a child support calculation on gifts the obligor father had historically received from his wealthy parents.

**Retirement Plan
Benefits**

RETIREMENT PLAN BENEFITS

A. *Kennedy v. Plan Admin. for DuPont SIP* (2009) 129 S.Ct. 865: Wife's Marital Settlement Agreement waiver of her interest in Husband's ERISA SIP plan was not a prohibited assignment or alienation; however, since Husband had not named another beneficiary, the plan properly paid benefits to her.

B. *Carmona v. Carmona* (2008) 544 F.3d 988: Waiver language in a Marital Settlement Agreement is insufficient to allow a Court to replace a former spouse locked in as beneficiary of post-retirement survivor benefits (QJSA) under an ERISA-regulated plan where the participant retired and an annuity had become payable during a prior marriage.

C. *Regents of U.C. vs. Benford* (2005) 128 Cal.App.4th 867: A Non-employee spouse who predeceases an employee spouse cannot bequeath their community property interest in UC pension plan benefits; Family Code section 2610 is inapplicable when a non-employee spouse dies before property is divided in a divorce or legal separation proceeding.

There are three (3) cases now pending before the California Supreme Court involving what is known as the "California rule," which concerns the issue of modification of Public Employee Pensions v. the vested rights of public employees. The cases are as follows:

1. *Cal Fire Local 2881 v. California Public Employees Retirement System* (2016) 7 Cal.App.5th 115;

2. *Marin Association of Public Employees v. Marin Association of Public Employees Retirement Association* (2016) 2 Cal.App.5th 674;

3. *Alameda County Deputy Sheriffs Association v. Alameda County Employees Retirement Association* (2018) 19 Cal.App.5th 61.

In 2012, the California Legislature enacted certain pension reforms which public employee unions and others challenged as violating the vested rights of public employees to their pensions. The "California rule," a public employee's right to receive a future pension benefit on fixed terms, has been considered a vested right, meaning that those terms can only be changed to the detriment of the employee under limited circumstances. The California Supreme Court has before it three cases, cited above, in which the parties and Amici have advanced arguments applicable to determining the proper scope of the "California rule." In counsel's initial examination and evaluation of the pension rights of public employees, the three cases should be carefully mentioned.

ALTERNATIVE DISPUTE RESOLUTION–MEDIATION CONFIDENTIALITY

A. *Lappe v. Superior Court* (2014) 232 Cal.App.4th 774: For many years, California courts have held that anything and everything taking place in mediation is absolutely privileged. In the *Lappe* case, the Court of Appeal held that the mediation confidentiality statute, Evidence Code section 1119(b), does not apply to financial disclosure declarations exchanged during mediation. The court reasoned that financial disclosure declarations are not protected by the mediation privilege because they are prepared for the purpose of complying with the Family Code's statutory mandate, not for the purpose of mediation. The mere introduction of financial disclosure declarations in a mediation does not shield those declarations from discovery. The Court of Appeal further held that the stipulation of the parties that the financial disclosure declarations would be inadmissible was an erroneous attempt to restrict the trial court's authority to receive the declarations of disclosure into evidence in a motion to set aside the judgement. This case involved a clash of two competing public policy considerations; mediation confidentiality versus full disclosure in family law litigation. This is one of the few cases that, while not containing a judicial exception to mediation confidentiality, held that in this instance, mediation confidentiality did not apply. The California Supreme Court denied review of the case on March 11, 2015.

B. *Simmons v. Ghaderi* (2008) 44 Cal.4th 570: The Court of Appeal improperly relied on estoppel to create a judicial exception to the statutory scheme of mediation confidentiality. Evidence regarding mediation is not admissible; implied waiver does not apply to mediation confidentiality.

C. *In re Marriage of Kieturakis* (2006) 138 Cal.App.4th 56: Husband did not bear the burden of proof on Wife's motion to set aside a mediation-based Marital Settlement Agreement where she refused to waive the mediation privilege; the presumption of undue influence in mediated marital transactions must yield to policies favoring mediation and finality of judgments.

D. *Doe I* (2005) 132 Cal.App.4th 1160: Disclosure of written personnel summaries prepared through the mediation process was barred by the mediation confidentiality privilege under Evidence Code section 1122(a)(2). While disclosure of specific, written summaries was barred, underlying information used to prepare the summaries, was not prohibited from being released to the public.

E. *Rojas v. L.A. Super. Ct. (Coffin)* (2004) 33 Cal.4th 407: Evidence Code section 1119 absolutely protects "writings" prepared for mediation, including photos, videos, and factual material.

F. *Eisendrath v. Super. Ct. (Rogers)* (2003) 109 Cal.App.4th 351: Confidential mediation communications may not be disclosed without parties' express waiver; a mediator is incompetent to testify under Evidence Code section 703.5.

CAPACITY TO ENTER INTO BINDING AGREEMENTS

Attachment 3 is *California Lawyer's Grey Fog of Uncertainty: Assessing a Client's Diminished Mental Capacity*, California Family Monthly, November 2014, and also found in Estate Planning 2012 (UCLA School of Law and California Continuing Education of the Bar) pg. 383.

A. *Lintz v. Lintz* (2014) 222 Cal.App.4th 1346: A wealthy decedent's third wife was found to have committed financial elder abuse (Welfare and Institutions Code section 15610.30), and there was a finding of undue influence, breach of fiduciary duty, and conversion of husband's separate property. Lois Lintz, was the third wife of Decedent, Robert Lintz. They were married in 1999, divorced six months later, and remarried in February 2005. Mr. Lintz passed away in October 2009 at the age of 81. At the time they remarried, he was a retired real estate developer worth millions of dollars. Mr. Lintz had a complicated estate plan with holdings in northern and southern California. His northern California estate plan was contained in the Robert Lintz Trust and a series of amendments prepared over the years by his estate lawyers. The Ninth Amendment to the trust, prepared at the time Mr. and Mrs. Lintz remarried, designated Mr. Lintz' children, grandchildren, and former son-in-law as beneficiaries. Three months after their remarriage in 2005, Mr. Lintz executed a Tenth Amendment to the trust, providing Mrs. Lintz with 50% of his assets upon his death, with 50% being distributed among Mr. Lintz' children and grandchildren. Between 2005 and 2008, Mr. Lintz executed several additional amendments to the trust, increasingly providing Mrs. Lintz with more of his assets and disinheriting his two eldest children. In June 2008, Mr. and Mrs. Lintz executed the Lintz Family Revocable Trust, prepared by Mrs. Lintz' attorney, designating all of Mr. Lintz' property as community property, gave Mrs. Lintz an exclusive life interest in his estate, and gave Lois the right to disinherit Mr. Lintz' youngest child and leave any unspent residue to his two eldest children.

Upon Mr. Lintz' death, his two eldest children, as successors in interest, filed a complaint against Mrs. Lintz alleging several causes of action, including fiduciary abuse of an elder, breach of fiduciary duty, conversion, constructive trust, and undue influence. The Probate Court found her liable for financial elder abuse under Welfare and Institutions Code section 15610.30, breach of fiduciary duty and, conversion of separate property funds, further finding Mrs. Lintz as constructive trustee of Mr. Lintz' converted funds and trust property. Although decedent had testamentary capacity, Mrs. Lintz was held liable for undue influence in the procurement of Mr. Lintz' estate plans. The Probate Court voided all trusts and trust amendments following the 2005 Tenth Amendment to the trust, invalidated real property deeds, and took steps to implement the terms of the Tenth Amendment.

Although the Probate Court applied the incorrect standard for legal capacity and failed to apply a presumption of undue influence to interspousal transactions, the Probate Court's judgment voiding Decedent's testamentary trusts and trust amendments was amply supported by evidence.

First, the Court of Appeal considered whether the Probate Court properly applied the Probate Code section 6100.5 testamentary capacity standard to Mr. Lintz' trust and trust amendments at issue, instead of the sliding-scale contractual standard in Probate Code sections 810 through 812. Section 6100.5 contemplates a significantly lower mental capacity standard and applies to the mental capacity to make a will. Trusts often involve more complicated issues and may require a higher standard of mental capacity. Thus, courts apply a sliding scale, as dictated by Sections 810 through 812, depending on the complexity of the issues. Since these transactions were quite complex, the sliding scale should have been applied. (See *Anderson v. Hunt* (2011) 196 Cal.App.4th 722, 730.) However, since the transactions were voided based upon the lower standard, the error was harmless.

Second, the Court of Appeal held that Family Code section 721, which imposes a fiduciary duty between spouses, applied since the trust amendments were marital transactions. Therefore, the Probate Court should have applied the presumption of undue influence with respect to Mr. Lintz' transmutation of separate property to community property, the huge sums of money he transferred to Mrs. Lintz and to the Lintz Family Revocable Trust [designating all of Mr. Lintz' property as community property, giving Mrs. Lintz an exclusive life interest in his estate, and giving Mrs. Lintz the right to disinherit Mr. Lintz' youngest child and leave any unspent residue to his two eldest children] thereby shifting the burden to Mrs. Lintz to rebut the presumption. Even without that burden, Mrs. Lintz did not rebut the presumption of undue influence. The Court of Appeal recognized that undue influence could be proven by circumstantial evidence; plaintiffs were not required to produce direct evidence. Circumstantial evidence of undue influence here was extensive.

B. *In re Marriage of Greenway* (2013) 217 Cal.App.4th 628: In the *Greenway* case, after a 48 year (!) marriage, Lyle (76) sought to end his marriage to Joanne (72); she contended that Lyle was mentally incompetent and incapable of making a reasoned decision regarding his marital status. After taking extensive evidence, the retired judicial officer serving as the trial judge determined that Lyle was in fact mentally capable of making a reasoned decision to end the marriage and granted his request for a status-only dissolution. In affirming, the Court of Appeal determined that the mental capacity required to end one's marriage is similar to the mental capacity required to enter into the marriage, i.e., the baseline presumption of mental capacity is based upon the criteria set forth in Probate Code section 811 (part of the Due Process in Competence Determinations Act). As framed by the appellate opinion, notwithstanding the fact that the testifying experts agreed that Lyle had dementia, the question was whether his impairment was such that he no longer had the capacity of making a reasoned decision to end his marriage. In analyzing conflicting arguments, the Court of Appeal determined that a person's mental capacity is fact-specific, and the level of required mental capacity changes depending on the issue at hand. Complicating matters are the multiple and overlapping statutes regarding the "capacity" of elders (those over the age of 65) found in the Probate Code, the Welfare and Institutions Code, the Civil Code and the Family Code. The *Greenway* court concluded that mental capacity can be measured on a sliding scale, with mental capacity requiring the least amount of capacity, followed up the scale by testamentary capacity, and, on the high end of the scale, the mental capacity required to enter into contracts. Thus, the burden of proof with respect

to mental capacity changes depending on the issue presented.

There exists a presumption in favor of a person seeking to marry or make a will, “but not so in the context of a person executing a contract.” In its summary of overlapping statutes with varying semantics relating to mental capacity, the court held that the required level of understanding rests entirely on the complexity of the decision being made; case authority evidences an extremely low level of mental capacity needed before the decision to marry or to execute a will. Similarly, the standard for testamentary capacity is also relatively low; however, the capacity to contract, which includes the capacity to convey, create a trust, make gifts and to grant powers of attorney, requires the baseline criteria contained in Probate Code sections 811 and 812, as well as the specific guidelines for determining the capacity to contract embraced in Civil Code section 39(b).

As our society ages, these issues acquire a more nuanced complexity. *In re Marriage of Straczynski* (2010) 189 Cal.App.4th 531, saw the appellate court hold that an incapacitated individual may *maintain* a dissolution proceeding only if he or she remains capable of exercising a judgment, and expressing a wish, that the marriage be dissolved throughout the proceeding. In that case, the conservatee had to be capable of making the decision to file the Petition and expressing her desire to end the marriage. *Anderson v. Hunt* (2011) 196 Cal.App.4th 722, was a case where the Court of Appeal held that where a person simply amends a trust, that person’s capacity should be determined by the lower standard of executing a will, as set forth in Probate Code section 6100.5.

The *Greenway* opinion pointed out that the level of dementia was not the factual issue being decided by the trial court. It was not a conservatorship proceeding. The sole issue before the court was whether or not Lyle had the required level of mental capacity, despite his diagnoses of dementia, to end the marriage. Lyle was found to have had the requisite capacity. *Greenway* is a lengthy opinion, but is worthy of careful review to remind and sensitize counsel to the legal, ethical and emotional components of this increasingly prevalent mental health issue.

Family Law and Estate Planning Crossover Issues

Paul Gordon Hoffman
Hoffman, Sabban & Watenmaker, APC

Marshall Zolla
Law Offices of Marshall S. Zolla,
A Professional Corporation

I. Introduction.

Family law lawyers and estate planning lawyers routinely face the same questions. Is a client really married (which may turn on whether a prior marriage was validly terminated,) and if not, whether the “putative spouse” rules apply to create “quasi-marital property”? Is an asset community property, separate property, or some mixture of each? If separate property and community property is mixed, is there merely a right of reimbursement without interest, or is there a sharing of appreciation? What is required for a valid “transmutation” to occur? What actions can be taken when one spouse lacks (or arguably lacks) capacity? What is the extent of the fiduciary duties between the spouses? What marital property laws apply when one spouse lives in California and the other spouse lives in New York? Is a pre-marital agreement binding on the spouses?

Family law lawyers and estate planning lawyers also routinely have an impact on the work of the other. A pre-marital agreement may have implications upon marital dissolution or on death. An irrevocable insurance trust created for the benefit of a spouse for estate planning purposes may complicate the situation when the marriage dissolves. A property agreement entered into during marriage may or may not be effective. When a couple divorces, the marital settlement agreement or judgment may contain terms that an estate planning lawyer would never want, such as a provision requiring that life insurance proceeds be paid to the minor children rather than to a trust for the benefit of the children. When one spouse files for divorce in California, Automatic Temporary Restraining Orders go into effect that limit the ability of each spouse to make changes to their estate plans, including changes affecting their separate property. What obligations might a family law lawyer have to get his client to amend his or her estate plan and beneficiary designations, either upon filing (subject to the ATROs) or when the dissolution is complete?

These issues could take up a full day program, and today’s presentation will focus on only a few of them. Note that the same issues that we’re discussing regarding married couples will also apply, in general, to Registered Domestic Partners.

II. Prenuptial Agreements.

A. California has extensive statutory and case law regarding prenuptial agreements. See generally California Family Code sections 1610-1617.

B. Who is qualified to prepare a prenuptial agreement? Should an estate planning lawyer participate in the drafting of a prenuptial agreement without the involvement of a family law lawyer? Should a family law lawyer participate in the drafting of a prenuptial agreement without the involvement of an estate planning lawyer? Do those lawyers have sufficient tax knowledge to properly evaluate the proposed agreement?

C. Is a prenuptial agreement necessary to protect a spouse's premarital separate property? If the spouses are currently living in California, must you anticipate the possibility of their moving to another jurisdiction that provides for "equitable division" on divorce, or a "statutory share" on death?

D. How can you get an agreement signed without destroying the proposed marriage? When is an agreement fair? Does it matter?

E. When does the agreement have to be presented to the other party and when does it have to be signed in order for the agreement to be effective (both as to property rights and as to spousal support waivers)? Family Code Section 1615(c)(2) provides that among the requirements to find that an agreement was entered into voluntarily is that, "The party against whom enforcement is sought had not less than seven calendar days between the time that party was first presented with the agreement and advised to seek independent legal counsel and the time the agreement was signed." *In re Marriage of Caldwell-Faso*, (1st Dist. 2011) 191 Cal.App.4th 945, held that the seven day period did not apply when both parties have been represented by counsel during negotiations leading up to the drafting of the agreement.

F. What financial disclosures must be made, or what access to information must be provided? *In Marriage of Hill & Dittmer* (2011) 202 CA4th 1046, the court upheld an agreement where there was a lack of disclosure because it determined that the other spouse had waived disclosure both in the agreement and in her conduct during the negotiations.

G. Note that spousal support waivers must not be unconscionable, both at the time the agreement is entered into, and when enforcement is sought, and the supported party must be represented by independent counsel. Family Code Section 1612(c). See *In re Marriage of Facter* (2013) 212 Cal.App.4th 967 for a discussion of what constitutes an unconscionable agreement, and for a discussion of agreements that predate the current statute.

G. What issues commonly arise in connection with a prenuptial agreement?

Characterization of earnings and assets as community property or separate property (including waivers of Van Camp/Pereira transmutations (*Van Camp v. Van Camp*, 199 P. 885 (California, 1921); *Pereira v. Pereira*, 103 P. 488 (California, 1909))

Management and control of assets

Spousal support

Retirement Equity Act (ERISA) waivers

Transfers from one spouse to the other
Gifts between spouses and gifts to third parties
Possession of the home upon separation
Provisions governing transfers upon death of either spouse
Filing joint or separate income tax returns

NOTE: Provisions regarding support of children and custody generally cannot be made binding by a prenuptial agreement. (See Family Code section 1612(b) re child support). Provisions regarding the religious upbringing of the children are likely invalid.

III. Marital Property (post-nuptial) Agreements

A. Lack of California statutory and case law on post-nuptial agreements. Family Code sections 1610-1617 has extensive provision regarding premarital agreements. Family Code section 850 allows a married couple to transmute the character of assets, and pursuant to Family Code section 853, it must be in writing. Family Code section 1500 provides that the property rights of husband and wife prescribed by statute may be altered by a premarital agreement “or another marital property agreement.” Presumably, you could alter not only rights during marriage but also upon death (e.g., a waiver of inheritance rights under a retirement plan.) As with a premarital agreement, you can’t bind the court with respect to child support or visitation.

B. Can spousal support be waived in a post-nuptial agreement? Can a post-nuptial agreement validly modify spousal support provisions in an otherwise valid pre-nuptial agreement? California Family Code section 1620 provides, “Except as otherwise provided by law, a husband and wife cannot, by a contract with each other, alter their legal relations, except as to property.”

C. Fiduciary duties owed to a spouse, as opposed to a potential spouse; need for separate representation.

D. A document that purports to transmute separate property to community property is fraught with malpractice risk for the lawyer who prepares it. Despite a written conflict waiver, the conversion of one spouse’s separate property assets to community property probably raises an actual (not just potential) conflict of interest. Thus, each spouse should be separately represented. Also, the impact of a transmutation on a division of the assets in a divorce must be explained. A presumption of undue influence arises against the benefitted spouse, which may or may not be overcome in a subsequent dissolution action. See *Marriage of Lico* (Filed 5/4/2012, 1st Dist. Ct. of Appeal), case A130765 (unpublished). (Note that the agreement clearly provided that each spouse was making a gift of one-half of that party’s separate property to the other spouse, and waived a right of reimbursement, but the agreement was found to be unenforceable based on husband’s claim that he didn’t understand that the agreement was irrevocable when he thought that the entire estate plan was revocable.)

E. A single sentence in a trust agreement stating that all assets in the trust are community

is insufficient to effect a valid transmutation. *Marriage of Starkman* (2005) 129 Cal.App.4th 659, 664.

F. You can't treat assets as community property on death but as separate property for marital dissolution purposes. *Marriage of Lund* (2009) 174 CA4th 40, 52, 94 CR3d 84, and *Marriage of Holtemann* (2008) 166 CA4th 1166, 1173, 83 CR3d 385.

G. In *In re Marriage of Valli* (2014) 58 C4th 1396, the California Supreme Court held that a life insurance policy purchased by Frankie Valli, owned by his wife, was community property in the absence of a writing signed by him transmuting the policy to the wife's separate property.

IV. Capacity to Marry and Divorce, and Inter-Spousal Transactions.

A. A conservatee can marry without the need for the consent of the conservator, absent a court order to the contrary; but the court can determine if the conservatee has capacity to marry. Probate Code sections 1900 & 1901; Family Code section 301. A party to the marriage can bring an action to determine the validity of the marriage, and presumably the conservator could bring such an action on behalf of the conservatee. Family Code section 309. The conservator may seek to set aside a marriage due to lack of capacity. Family Code 2211 (c).

B. A conservator can bring an action for marital dissolution, if the conservatee is capable of exercising a judgment and expressing a wish that the marriage be dissolved. *In re Marriage of Higgason*, 10 Cal.App. 3d 476 (1973). If a spouse sues for dissolution on the grounds of "incurable insanity", the conservator must defend the conservatee. Family Code section 2332.

C. In *Marriage of Greenway*, 217 Cal.App 4th 628 (2013), the court held that the degree of mental capacity required to divorce is similar to that required to marry. This is an extremely low standard. In making its ruling, the court looked to the Probate Code standard for testamentary capacity (Probate Code section 6100.5) and the Civil Code rules on contract (Civil Code section 39).

D. For a nice analysis of *Greenway* and other cases on this topic, see Klein & Green, "Undoing Capacity", Los Angeles Lawyer 33, July/August 2014, available at <http://www.lacba.org/Files/LAL/Vol37No5/3179.pdf>.

E. In *Lintz v. Lintz*, 222 Cal.App.4th 1346 (2014), the court set aside a transmutation of separate property to community property, and provisions for a spouse under a living trust. The court held that Family Code section 721 imposes a fiduciary duty between spouses, and the Probate Court should have applied a presumption of undue influence. The court also held that the Probate Court should have applied the "sliding scale" standard of contractual capacity (based on the complexity of the documents) under Probate Code sections 810 to 812, rather than the testamentary capacity standard of Probate Code section 6100.5.

F. *In re Marriage of Woolsey* (2013) 220 CalApp4th 881 held that there is no presumption of undue influence in a marital settlement agreement reached as the result of mediation.

F. For further reading on the scope of a lawyer's duties in connection with representation of a couple for estate planning, see *Guide to the California Rules of Professional Conduct for Estate Planning, Trust and Probate Counsel, Third Edition*, published by the State Bar of California Trusts & Estates Section, available at <http://trustslaw.calbar.ca.gov/Publications/EthicsGuide.aspx>. Note that a joint representation legal services agreement should clearly provide that the attorney will disclose information learned from one spouse, to the other spouse, if significant to the other spouse.

V. ATROs and Estate Planning During a Marital Dissolution.

A. Upon filing for a marital dissolution, the person filing is restrained by ATROs, and upon being served, the other party is also restrained by ATROs. See Family Code section 2040.

B. What can, or cannot, be done once the ATROs come into effect?

1. You can change your Will, without notice, without spousal approval and without court approval. Among the things you can do in the new Will is name a different Guardian for your minor children in case the other parent predeceases, and a new Executor and Trustee.

2. You can't amend a trust unless you have the written consent of the other party or a court order, but you can revoke an existing revocable trust if you give prior notice. Note that Family Code Section 2040(b)(4) only prevents an amendment that affects the disposition of property, so presumably you could change the Trustee without consent of the other party or a court order.

(a) The restraint on amendment appears to apply to a purely separate property trust; but query why Family Code Section 2040(b)(2) (dealing with transfers of assets) speaks of "any property, real or personal, whether community, quasi-community, or separate" while Family Code Section 2040(b)(4) (dealing with amendment of non-probate transfers) is silent on the types of property covered?

(b) If you have a power of appointment over a trust that is exercisable by Will, then perhaps you can exercise that power of appointment, so you could do indirectly what you can't do directly (i.e., change the terms of a trust). However, it is possible that Family Code Section 2040(a)(4), referencing Non-Probate Transfers (defined in Family Code Section 2040(d)(1)), with the inclusion of Probate Code Section 5000, might be broad enough to encompass a power of appointment.

(c) As noted above, you can revoke a trust if you notify the other party in advance; and you can then make a will that disposes of your share of the assets even without notice to the other party.

(d) What is the public policy that restrains a person from changing their revocable living trust as to their separate property when they can do indirectly (albeit perhaps with notice to the spouse) what they can't do directly, by revoking the trust and signing a Will?

3. You can't fund a new trust (even with your clearly separate property) unless you have approval of the other spouse or the court.

(a) You can set up an unfunded trust and have the Will pour over to the unfunded trust, all without court or spousal approval.

(b) You may be able to draft a "springing" assignment of assets into the new trust that is effective upon the termination of the ATROs.

4. You can change your durable power of attorney and your Advance Health Care Directive, without court or spousal approval or notice.

5. You can change a joint tenancy WROS to a tenancy in common if you give notice to the other party; you don't need the consent of the spouse or the court. It appears that one spouse can unilaterally convert a community property WROS to a regular community property holding. Civil Code Section 682.1 says that, "Prior to the death of either spouse, the right of survivorship may be terminated pursuant to the same procedures by which a joint tenancy may be severed. Part I (commencing with Section 5000) of Division 5 of the Probate Code and Chapter 2 (commencing with Section 13540), Chapter 3 (commencing with Section 13550) and Chapter 3.5 (commencing with Section 13560) of Part 2 of Division 8 of the Probate Code apply to this property."

6. You can't change beneficiary designations on life insurance or retirement plan benefits or annuities, or other similar beneficiary designations (e.g., under an employment agreement, or a Guild assignment of residuals) even if it relates only to your separate property, without your spouse's consent or court order. **Why can you eliminate a right of survivorship with notice but without consent (and then leave assets by Will), but you can't change a beneficiary designation without approval of the spouse or court?** Note that under the Retirement Equity Act ("REACT"), a married person generally cannot eliminate benefits under a qualified retirement plan for the non-participant spouse without the written, informed and notarized consent of the non-participant spouse. REACT does not apply to IRAs.

7. You can't change the beneficiary on any other asset (e.g., creating a Totten Trust or POD account), even if it relates only to your separate property, without your spouse's consent or court order.

8. You can disclaim assets left to you by a third party.

9. You can't make gifts, even of your clearly separate property, even to the kids, without your spouse's consent or court order. However, if there is a pattern and practice of making gifts (say, annual gift to children, or paying school tuition for grandchildren, or supporting an incapacitated parent), is there an exception for transfers "in the ordinary course"?

10. If you bifurcate the divorce, you can remarry, in which case your new spouse will have rights in your assets upon your death unless you have a prenuptial agreement or sign a new Will. Of course, in the bifurcation, the Retirement Equity Act implications on retirement plan benefits must be taken into account. See Family Code section 2337 regarding the matters over which jurisdiction will remain with the court pending the final adjudication of property matters; and note that a number of other issues will probably be agreed to by counsel.

C. You can change your estate planning BEFORE anyone files for dissolution of the marriage and thus before the ATROs come into effect.

D. What is the effect of a violation of the ATROs? Does it make a difference if the only person affected is someone OTHER THAN the spouse or a minor child? Suppose, for example, that you change your estate plan in a manner that does not affect the spouse (e.g., leave more to the adult children of your prior marriage and less to the adult children of the current marriage)? Is it void? Is it voidable? Family Code Section 2010 provides that the Court has no jurisdiction over a spouse's separate property, but there could be issues as to whether there is a community property element to what is otherwise separate property (e.g., a Van Camp/Pereira argument or use of community to improve or make principal payments on separate property). A Law Revision Commission option (not adopted) would have limited the restrictions where there was a prenuptial agreement or post-nuptial agreement in effect that eliminates all community property. California Law Revision Commission Study FHL-911; First Supp. To Memo 99-84; Rel. 1-19-00. See *Allstate Life Ins. v. Dall*, below.

E. If you revoke a trust (e.g., a separate property trust), but don't change the title to the assets held in the trust, can you "unrevoke" the trust after the ATROs are lifted?

F. For a nice summary of the rules on ATROs, see Crum & Schoknecht, "How Can My Divorcing Clients Plan Their Estates with the ATROs in the Way?", available at <http://www.hansonflg.com/articles/detail/136>.

VI. What is the impact of divorce on estate planning documents?

A. Powers of attorney are revoked by divorce and revived by remarriage. California Probate Code section 4154. Similarly, advance health care directives are revoked by divorce and revived by remarriage. California Probate Code section 4697.

B. Pursuant to California Probate Code section 5600, in general, nonprobate transfers (other than life insurance beneficiary designations, but specifically including a provision of a document, other than a Will, that grants a power or appointment or names a trustee) are revoked by divorce. It appears that this provision applies to a revocable trust, but not an irrevocable trust.

1. Revocation does not occur in any of the following cases:

(a) The nonprobate transfer is not subject to revocation by the transferor at the time of the transferor's death.

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

(c) A court order that the nonprobate transfer be maintained on behalf of the former spouse is in effect at the time of the transferor's death.

2. *Kennedy v. Plan Administrator for DuPont Savings & Investment Plan*, 129 S. Ct. 865, 555 U.S. 285 (2009) holds that a plan administrator is free to pay out benefits based on the beneficiary designation on hand notwithstanding a prior court order or state law to the contrary. A Qualified Domestic Relations Order would have made the Plan a party to the action and would have resulted in the plan being bound by the terms of the Order.

3. *Allstate Life Ins. v. Dall*, 2009 U.S. Dist. LEXIS 100401 (E.D. Cal. 2009) held that a beneficiary designation change filed with the insurance company by husband while the ATROs were in effect was ineffective as a beneficiary designation. (The original designation named wife as primary beneficiary, with children as contingent beneficiaries.) After the beneficiary change form was signed, the parties entered into a Marital Settlement Agreement that waived the rights as beneficiary in the other spouse's life insurance. Thus, the court found the wife had "disclaimed" her right as a beneficiary, and the benefits passed to the children as contingent beneficiaries under the original designation.

C. Joint tenancies generally are revoked by divorce pursuant to California Probate Code section 5601.

1. Revocation does not occur if the joint tenancy is not subject to severance at the decedent's death.

2. Revocation does not occur if there is "clear and convincing evidence" that the decedent intended to preserve the rights of the former spouse.

D. Provisions in a Will for the benefit of the ex-spouse are revoked by divorce unless the Will expressly provides otherwise.

1. This includes dispositions or appointments in favor of the ex-spouse.

2. This includes the grant of a power of appointment to the ex-spouse

3. This includes a provision nominating the spouse as a fiduciary.

4. The provisions for the spouse are revived by remarriage.

E. Irrevocable trusts could be modified or termination by court order.

VII. Death During A Dissolution Action

A. Death prior to the entry of a judgement terminating the marital status causes the Family Court to lose jurisdiction. *Bevelle v. Bank of America* (1947) 80 Cal. App. 2d 333; *In re Marriage of Shayman*, (1973) 35 Cal. App. 3d 648. However, if the Family Court has already issued a judgment, the judgment may be entered. Code of Civil Procedure section 669. Thus, for example, the court could not issue a new order to determine the character of assets, award support, or grant fees or costs if those matters had not already been determined as of the date of death.

B. Death after entry of the judgment terminating marital status can have a different result. Family Code section 2344. Under Family Code section 2337(c), the court, as a condition of granting a bifurcation, can enter a broad range of orders (including “any other condition the court determines is just and equitable”, Section 2337(c)(10)) that remain binding after a party’s death. Subject to the effect of those orders, the probate court has jurisdiction over the estate of the deceased party.

VIII. Impact of Death on Support Orders

A. Generally, spousal support will terminate on the death of either spouse. Family Code section 4337. This condition is required to have the payments be deductible to the payor and taxable to the recipient.

B. Generally, the obligation to pay child support survives the death of the payor and is a liability of the payor’s estate, whether the decedent is the custodial parent (*In re Marriage of Gregory*, 230 Cal. App. 3d 112 (1991) or noncustodial parent (*Taylor v. George* (1949) 34 Cal. 2d 552, 556; *Stein v. Hubbard* (1972) 25 Cal. App. 3d 603, 605). The parents cannot agree between themselves to modify or terminate a support order. (*Armstrong v. Armstrong*, (1976) 15 Cal. 3d 942, at p. 947.) The supported parent is a creditor and must file a claim against the estate of the deceased parent. On the other hand, the estate can seek to modify the child support order, even after the obligor’s death. See dicta in *Stein v. Hubbard*, 25 Cal. App. 3d 603 (1972). The better practice is to provide in the estate plan that any child support obligation will be charged against the share of the estate going to the child with respect to whom the support is being paid.

LAW OFFICES

MARSHALL S. ZOLLA

A PROFESSIONAL CORPORATION
2029 CENTURY PARK EAST
SUITE 1020

LOS ANGELES, CALIFORNIA 90067-2911

TELEPHONE (310) 407-0770

FACSIMILE (310) 407-0776

MARSHALL S. ZOLLA*†‡
DEBORAH ELIZABETH ZOLLA
VIVIAN CARRASCO HOSP

*CERTIFIED SPECIALIST - FAMILY LAW
THE STATE BAR OF CALIFORNIA
BOARD OF LEGAL SPECIALIZATION

†A PROFESSIONAL CORPORATION

‡ FELLOW, AMERICAN ACADEMY OF
MATRIMONIAL LAWYERS
WWW.ZOLLALAW.COM

OF COUNSEL

JOEL P. SCHIFF*†
KEHR, SCHIFF & CRANE LLP

*CERTIFIED SPECIALIST - APPELLATE LAW
THE STATE BAR OF CALIFORNIA
BOARD OF LEGAL SPECIALIZATION
†ALSO ADMITTED IN THE STATE OF NEW YORK

MARSHALL S. ZOLLA
CURRICULUM VITAE

EDUCATION

UNIVERSITY OF CALIFORNIA, LOS ANGELES
(A.B. *CUM LAUDE*, ECONOMICS, 1960)

BERKELEY LAW
UNIVERSITY OF CALIFORNIA,
BERKELEY, SCHOOL OF LAW
[BOALT HALL]
(J.D., 1963)

ADMITTED TO PRACTICE IN CALIFORNIA, 1964

CERTIFICATION

CERTIFIED SPECIALIST - FAMILY LAW, BOARD OF LEGAL SPECIALIZATION OF THE STATE BAR
OF CALIFORNIA

LAW FIRM

LAW OFFICES
MARSHALL S. ZOLLA
A PROFESSIONAL CORPORATION
LOS ANGELES, CALIFORNIA

AV RATING:

MARTINDALE-HUBBELL NATIONAL LAW DIRECTORY
MARTINDALE-HUBBELL BAR REGISTER OF PREEMINENT LAWYERS [1997 - 2018]

AMERICAN ACADEMY OF MATRIMONIAL LAWYERS

FELLOW, AMERICAN ACADEMY OF MATRIMONIAL LAWYERS

PUBLICATIONS

- ◆ EDITORIAL CONSULTANT AND COMMENTATOR, CALIFORNIA FAMILY LAW MONTHLY, MATTHEW BENDER & COMPANY, 1988 - 2018
- ◆ AUTHOR: *GAME CHANGER: IN PEOPLE V. SANCHEZ, THE CALIFORNIA SUPREME COURT CHANGED THE RULES OF ADMISSIBLE EXPERT TESTIMONY*, CALIFORNIA FAMILY LAW MONTHLY, SEPTEMBER 2017
- ◆ AUTHOR: *INCORPORATING PERSONAL VALUES INTO ADVANCE HEALTHCARE DIRECTIVES*, LOS ANGELES LAWYER, OCTOBER 2015
- ◆ AUTHOR: *THE CALIFORNIA LAWYER'S GREY FOG OF UNCERTAINTY: ASSESSING A CLIENT'S DIMINISHED MENTAL CAPACITY*, UPDATED AND REPRINTED, CALIFORNIA FAMILY LAW MONTHLY, NOVEMBER 2014
- ◆ CO-AUTHOR: *MEDIATION CONFIDENTIALITY VS. BREACH OF SPOUSAL FIDUCIARY DUTY: THE CLASH OF ENSHRINED PUBLIC POLICY TITANS*, CALIFORNIA FAMILY LAW MONTHLY, JUNE 2012
- ◆ AUTHOR: *THE CALIFORNIA LAWYER'S GREY FOG OF UNCERTAINTY: ASSESSING A CLIENT'S DIMINISHED MENTAL CAPACITY*, UNIVERSITY OF CALIFORNIA, LOS ANGELES/CONTINUING EDUCATION OF THE BAR TAX & ESTATE PLANNING CONFERENCE, MAY 2012; U.S.C. TAX AND PROBATE INSTITUTE 37TH ANNUAL TRUST AND ESTATE CONFERENCE, NOVEMBER 2011
- ◆ AUTHOR: UCLA SCHOOL OF LAW, AND CEB ESTATE PLANNING CONFERENCE 2012, CHAPTER 9, FAMILY LAW AND ESTATE PLANNING CROSSOVER ISSUES
- ◆ AUTHOR: PUBLICATION OF CHAPTER IN NATIONWIDE BOOK PUBLISHED BY ASPATORE BOOKS ENTITLED *INSIDE THE MINDS: STRATEGIES FOR FAMILY LAW IN CALIFORNIA*, 2011 EDITION, CHAPTER TITLE: EVOLVING FAMILY LAW ISSUES AND STRATEGIES
- ◆ CO-AUTHOR: PUBLICATION OF CHAPTER IN CEB PUBLICATION ENTITLED *DIVIDING PENSIONS AND OTHER EMPLOYEE BENEFITS IN CALIFORNIA DIVORCES*. CHAPTER 2, *INITIAL PROCEDURES AND PRETRIAL ORDERS*, JANUARY 2007; SUPPLEMENT, 2009
- ◆ CO-AUTHOR: PUBLICATION OF CHAPTER ON *FIDUCIARY DUTY BETWEEN SPOUSES IN THE 2008 FAMILY LAW SYMPOSIUM REFERENCE BOOK*, LOS ANGELES COUNTY BAR ASSOCIATION, MAY 2008

- ◆ PRACTICE CONSULTANT, CALIFORNIA FAMILY LAW LITIGATION GUIDE, MATTHEW BENDER & COMPANY
- ◆ CO-AUTHOR: *AUTOMATIC TEMPORARY RESTRAINING ORDERS [ATROS]: PROTECTOR OF THE STATUS QUO OR IMPERMISSIBLE RESTRAINT ON ALIENATION?*, CALIFORNIA FAMILY LAW MONTHLY, NOVEMBER 2005
- ◆ CO-AUTHOR: *MARITAL DUTY, FIDUCIARY DUTY BETWEEN SPOUSES*, COVER ARTICLE, LOS ANGELES LAWYER, FEBRUARY 2004
- ◆ CO-AUTHOR: *HEALTH CARE AND FAMILY LAW: AN UNHEALTHY ALLIANCE*, CALIFORNIA FAMILY LAW MONTHLY, JUNE 2003
- ◆ CO-AUTHOR: *RELIGIOUS DIVIDE: TIME FOR ANOTHER LOOK AT RELIGIOUS UPBRINGING PROVISIONS IN PRENUPTIAL AGREEMENTS*, CALIFORNIA LAWYER, JUNE 2002
- ◆ CO-AUTHOR: *LASTING WISHES: CALIFORNIA'S NEW HEALTH CARE DECISIONS LAW*, LOS ANGELES LAWYER, DECEMBER 2000
- ◆ AUTHOR: *AN INTERDISCIPLINARY APPROACH TO MODERN FAMILY LAW PRACTICE*, LOS ANGELES LAWYER, JULY/AUGUST 2000
- ◆ AUTHOR: *RELIGIOUS DIFFERENCES IN CHILD CUSTODY AND VISITATION DISPUTES*, LOS ANGELES LAWYER, NOVEMBER 1998
- ◆ CO-AUTHOR: *GUARDS OF THE HOUSE: AS AGENTS OF THE COURT, GUARDIANS AD LITEM FACE SUBSTANTIVE AND ETHICAL DILEMMAS IN FAMILY LAW PROCEEDINGS*, LOS ANGELES LAWYER, JULY/AUGUST 1997
- ◆ CO-AUTHOR: *PROMISES, PROMISES: ENFORCEABILITY OF A PRENUPTIAL AGREEMENT IN CALIFORNIA MAY FOUNDER ON THREE CONFLICTING STANDARDS OF LAW*, LOS ANGELES LAWYER, DECEMBER 1995
- ◆ CO-AUTHOR: *QUALIFIED MEDICAL CHILD SUPPORT ORDERS [QMCSO's]*, BEVERLY HILLS BAR ASSOCIATION, 1995
- ◆ CO-AUTHOR: *THE PERPETUATION OF SHATTERED HEARTS: THE DISTURBING CONFLICT BETWEEN DEPENDENCY COURT AND FAMILY LAW JURISDICTION*, LOS ANGELES LAWYER, JULY/AUGUST 1993
- ◆ CO-AUTHOR: *GUIDELINE CHILD SUPPORT: HOW TO GET 'OFF' THE MANDATORY GUIDELINE*, BEVERLY HILLS BAR ASSOCIATION, 1993

- ◆ CO-AUTHOR: *THE DIVERSITY OF CHILD CUSTODY PROCEEDINGS IN CALIFORNIA*, LOS ANGELES COUNTY BAR ASSOCIATION FAMILY LAW SYMPOSIUM REFERENCE BOOK, 1993
- ◆ CO-AUTHOR: "*CHILD CUSTODY PROCEEDINGS OTHER THAN IN MARITAL DISSOLUTION ACTIONS*", LOS ANGELES COUNTY BAR ASSOCIATION FAMILY LAW SYMPOSIUM REFERENCE BOOK, 1991, 1992
- ◆ EDITORIAL CONSULTANT, CALIFORNIA MARITAL SETTLEMENT AGREEMENT, CAL.DRAFT MASTER SERIES, MATTHEW BENDER & Co., 1990
- ◆ AUTHOR: *WHEN PARENTS CHANGE THEIR MINDS*, CALIFORNIA STATE BAR JOURNAL, JANUARY, 1985
- ◆ AUTHOR: *EVALUATION, DIVISION AND PROOF OF RETIREMENT PLAN BENEFITS INCIDENT TO A MARITAL DISSOLUTION PROCEEDING*, BEVERLY HILLS BAR ASSOCIATION ELEVENTH ANNUAL FAMILY LAW SYMPOSIUM, 1985
- ◆ EDITORIAL CONSULTANT: CALIFORNIA LEGAL SYSTEMS, DOMESTIC RELATIONS, PUBLISHED BY MATTHEW BENDER & Co., 1983
- ◆ AUTHOR: *TAX IMPLICATIONS OF LIVING TOGETHER: CLOSE ENCOUNTERS OF THE UNCERTAIN KIND*, BEVERLY HILLS BAR JOURNAL, SPRING, 1981 (REPRINTED BY CALIFORNIA CONTINUING EDUCATION OF THE BAR, ADVANCED FAMILY LAW SERIES, *SOLVING THE PROBLEMS OF UNMARRIED COUPLES*, OCTOBER, 1982)
- ◆ AUTHOR: *PRENUPTIAL AGREEMENTS AND FREEDOM OF CONTRACT IN CALIFORNIA*, CALIFORNIA STATE BAR JOURNAL, JANUARY, 1981
- ◆ CO-AUTHOR: *REPORT OF THE FAMILY LAW MEDIATION PROGRAM OF THE LOS ANGELES COUNTY SUPERIOR COURT*, BEVERLY HILLS BAR ASSOCIATION JOURNAL, SPRING, 1980

TEACHING, LECTURES AND CONSULTING

- ◆ GUEST SPEAKER
LOS ANGELES ESTATE PLANNING COUNCIL
LOS ANGELES, CA
TOPIC: TALES FROM THE TRENCHES: WHAT HAPPENS (IN THE REAL WORLD) WITH
END OF LIFE DECISIONS AND ADVANCE HEALTHCARE DIRECTIVES?
MARCH 28, 2018

- ◆ GUEST SPEAKER
BEVERLY HILLS BAR ASSOCIATION
TRUSTS & ESTATES AND FAMILY LAW SECTIONS
LOS ANGELES, CA
TOPIC: FAMILY LAW AND ESTATE PLANNING CROSSOVER ISSUES
JANUARY 16, 2018

- ◆ GUEST SPEAKER
U.S.C. 43RD ANNUAL TRUST AND ESTATE CONFERENCE
LOS ANGELES, CA
TOPIC: TALES FROM THE TRENCHES: WHAT HAPPENS (IN THE REAL WORLD) WITH
END OF LIFE DECISIONS AND ADVANCE HEALTHCARE DIRECTIVES?
NOVEMBER 3, 2017

- ◆ GUEST SPEAKER
LOS ANGELES COUNTY BAR ASSOCIATION 49TH ANNUAL FAMILY LAW SYMPOSIUM
LOS ANGELES, CA
TOPIC: EVOLVING DUTIES OF FAMILY LAW ATTORNEYS RE INFORMATION
TECHNOLOGY, ELECTRONIC EVIDENCE [ESI], AND CYBER SECURITY
MAY 6, 2017

- ◆ GUEST SPEAKER
GLASER WEIL FINK HOWARD AVCHEN & SHAPIRO LLP
LOS ANGELES, CA
TOPIC: THE INTERDISCIPLINARY NATURE OF SUBSTANTIVE FAMILY LAW ISSUES
APRIL 18, 2017

- ◆ GUEST SPEAKER
BREAKFAST WITH THE EXPERTS
LOS ANGELES JEWISH FOUNDATION "FAMILY AND ESTATE: PRENUPTIAL AND
POSTNUPTIAL AGREEMENTS, AND ESTATE PLANNING DURING DIVORCE"
SEPTEMBER 3, 2014; SEPTEMBER 10, 2014

- ◆ GUEST SPEAKER
RBZ LLP
LOS ANGELES, CA
TOPIC: IMPORTANT AND OFTEN OVERLOOKED ISSUES AND CONCERNS REGARDING
PRENUPTIAL AGREEMENTS, POSTNUPTIAL AGREEMENTS, TRANSMUTATION
AGREEMENTS AND SPOUSAL FIDUCIARY DUTIES
AUGUST 20, 2014

- ◆ GUEST SPEAKER
WILSHIRE BOULEVARD TEMPLE
KALSMAN INSTITUTE OF JUDAISM AND HEALTH & CEDARS-SINAI MEDICAL CENTER
JEWISH WISDOM AND WELLNESS: A WEEK OF LEARNING
LOS ANGELES, CA
TOPIC: ADVANCE HEALTH CARE DIRECTIVES: PRACTICAL AND SACRED DECISIONS
APRIL 23, 2013

- ◆ GUEST SPEAKER
LOS ANGELES COUNTY BAR ASSOCIATION FAMILY LAW SYMPOSIUM
LOS ANGELES, CA
TOPIC: E-DISCOVERY
MAY 19, 2012

- ◆ GUEST SPEAKER
UNIVERSITY OF CALIFORNIA, LOS ANGELES/CONTINUING EDUCATION OF THE BAR
TAX & ESTATE PLANNING CONFERENCE
LOS ANGELES, CA
TOPIC: FAMILY LAW AND ESTATE PLANNING CROSSOVER ISSUES
MAY 12, 2012

- ◆ GUEST SPEAKER
U.S.C. TRUST AND ESTATE CONFERENCE
LOS ANGELES, CA
TOPIC: FAMILY LAW AND ESTATE PLANNING CROSSOVER ISSUES
NOVEMBER 18, 2011

- ◆ NATIONAL TELEVISION INTERVIEW
CNBC PRIMETIME SPECIAL: "DIVORCE WARS"
MARCH 2011

- ◆ RETAINED AS CONSULTANT, FAMILY LAW EXPERT, BY OTHER ATTORNEYS
AND LAW FIRMS

- ◆ GUEST SPEAKER
ESTATE COUNSELORS FORUM
U.S. TRUST, BANK OF AMERICA PRIVATE WEALTH MANAGEMENT
TOPIC: FAMILY LAW AND ESTATE PLANNING CROSSOVER ISSUES
JANUARY 20, 2011

MARSHALL S. ZOLLA
A PROFESSIONAL CORPORATION

- ◆ GUEST SPEAKER
HEBREW UNION COLLEGE
NEW YORK, N.Y.
TOPIC: THE SYNAGOGUE AND COMMUNITY AS SUPPORT DURING
LIFE-THREATENING ILLNESS
OCTOBER 20, 2010
- ◆ GUEST SPEAKER
UCLA LAW SCHOOL
TOPIC: REPRESENTING CLIENTS IN MEDIATION FROM A FAMILY LAW PERSPECTIVE
OCTOBER 6, 2010
- ◆ GUEST SPEAKER
VENABLE LLP
TOPIC: THE INTERDISCIPLINARY IMPACT OF SUBSTANTIVE FAMILY LAW ISSUES
DECEMBER 8, 2009
- ◆ GUEST SPEAKER
FAMILY LAW STUDY GROUP
TOPIC: EVOLVING CONCEPT OF THE FIDUCIARY DUTY BETWEEN SPOUSES
JANUARY 9, 2007
- ◆ GUEST SPEAKER
WHITE ZUCKERMAN WARSAVSKY LUNA WOLF & HUNT STUDY GROUP
TOPIC: AUTOMATIC TEMPORARY RESTRAINING ORDERS [ATRO's]
JUNE 7, 2006
- ◆ GUEST PANELIST
CITY NATIONAL BANK
DIVORCE HOLLYWOOD STYLE
JULY 2005
- ◆ SPEAKER:
2002 ANNUAL MEETING OF THE STATE BAR OF CALIFORNIA
PRACTICAL AND SACRED DECISIONS AT THE END OF LIFE:
ADVANCE HEALTH CARE DIRECTIVES;
MONTEREY, CALIFORNIA, OCTOBER 10-13, 2002
- ◆ 2001 MARITAL PROPERTY PLANNING SYMPOSIUM: THE STATE BAR OF CALIFORNIA
ESTATE PLANNING, TRUST, PROBATE LAW AND FAMILY LAW SECTIONS;
SAN FRANCISCO/LOS ANGELES, JULY 13-14, 2001
- ◆ CONTINUING LEGAL EDUCATION PRESENTATIONS: LAW FIRMS, ACCOUNTING FIRMS,
BUSINESS MANAGERS, CALIFORNIA CONTINUING EDUCATION OF THE BAR [CEB],
CALIFORNIA CENTER FOR JUDICIAL EDUCATION AND RESEARCH [CJER]

- ◆ PANELIST: LOS ANGELES COUNTY BAR ASSOCIATION, TRUSTS AND ESTATES SECTION, "ESTATE PLANNING & PROBATE ISSUES ARISING IN THE CONTEXT OF SECOND MARRIAGES," APRIL 1996
- ◆ LACBA EMPLOYEE BENEFIT COMMITTEE OF THE TAXATION SECTION AND THE FAMILY LAW SECTION "EARLY RETIREMENT BENEFITS, A NEW HIDDEN ASSET: AN ANALYSIS OF THE *GRAM* CASE," FEBRUARY 1995
- ◆ PANELIST: BEVERLY HILLS BAR ASSOCIATION FAMILY LAW SYMPOSIUM, 1979, 1980, 1981, 1984, 1987, 1989, 1991, 1992, 1993, 1995
- ◆ PANELIST AND AUTHOR: LOS ANGELES COUNTY SUPERIOR COURT CHILD CUSTODY COLLOQUIUM, 1995
- ◆ SPEAKER: BEVERLY HILLS BAR ASSOCIATION CITIZENS LAW SCHOOL, 1991, 1993

PROFESSIONAL ASSOCIATIONS

- ◆ STATE BAR OF CALIFORNIA (MEMBER, SECTIONS ON: FAMILY LAW; REAL PROPERTY; LAW OFFICE MANAGEMENT)
- ◆ LOS ANGELES COUNTY BAR ASSOCIATION (MEMBER, SECTIONS ON: FAMILY LAW; REAL PROPERTY; LAW OFFICE MANAGEMENT)
- ◆ BEVERLY HILLS BAR ASSOCIATION (CHAIR, FAMILY LAW SECTION 1982-1983); MEMBER, BOARD OF GOVERNORS, 1983-1984)
- ◆ FELLOW, AMERICAN ACADEMY OF MATRIMONIAL LAWYERS
- ◆ ASSOCIATION OF CERTIFIED FAMILY LAW SPECIALISTS
- ◆ BERKELEY LAW ALUMNI ASSOCIATION
[FOUNDING PARTICIPANT AND CONTRIBUTOR TO BOALT HALL FAMILY LAW SOCIETY]
- ◆ MEDIATOR, FAMILY LAW DEPARTMENT, LOS ANGELES SUPERIOR COURT
- ◆ CHAIRPERSON, FAMILY LAW MEDIATION PROGRAM, LOS ANGELES SUPERIOR COURT, WEST DISTRICT, 1978 - 1980

Los Angeles Lawyer



FEBRUARY 2004, VOL. 26, NO. 11 / \$3.00

Los Angeles lawyers
Marshall S. Zolla and
Deborah Elizabeth Zolla
clarify the scope of
the fiduciary duty
between spouses

page 20

Marital Duty

EARN MCLE CREDIT

Employee
Witnesses in
Litigation

page 28

Song-Beverly
Requirements

page 10

The Learned
Intermediary
Doctrine

page 16

Online
Legislative
Research

page 40

By Marshall S. Zolla and Deborah Elizabeth Zolla

Marital Duty

Current state law often creates a

Hobson's choice when a spouse decides

between separate and community property

to fund an investment opportunity

There is no doubt that a fiduciary duty exists between spouses in California, but the scope of that duty has become a much debated legal issue. Changing standards emanating from the courts and arguably inconsistent legislative enactments have created great uncertainty as to what is or should be the governing standard of the fiduciary duty owed by one spouse to the other. Anything less than a careful and thorough reading of recently amended Family Code Section 721 will not shed clarifying light on whether the prudent investor rule does or does not apply between spouses. The current ambiguity in this regard has created frustration for lawyers and confusion for clients.

Recognition of a duty between spouses began over 40 years ago, with *Vai v. Bank of America*,¹ in which the California Supreme Court held that "because of his management and control over the community property, the husband occupies the position of trustee for his wife in respect to her one-half interest in the community assets." From then until today, courts and the legislature have twisted and turned in

their respective efforts to define an equitable standard of duty between spouses. In 1973, the court of appeal held that the fiduciary duty did not extend to all the husband's business dealings with community property but was to be limited to property settlements with his wife.² In 1975, the legislature enacted Civil Code Section 5125, which provided equal management and control of community property and reduced the spousal duty to "good faith."

In 1979, the California Supreme Court spoke again,³ this time to limit the period during which the spousal duty exists to the time prior to filing a petition for dissolution. As a result, the court held, "from the time that wife filed her petition seeking dissolution of the marriage...her relationship with her husband was an adversary one. Any obligation of trust between them [is] terminated."⁴ The supreme court held that the mere disclosure of an asset was sufficient and that further information regarding the nature or value of the asset was not necessary.⁵ Still, notwithstanding the end of an obligation of trust, in 1983, the court of appeal recognized that a duty of good faith re-

Marshall S. Zolla, a State Bar certified specialist in family law, practices in Century City. Deborah Elizabeth Zolla practices family law with the firm of Freid and Goldsman in Century City. The authors acknowledge the research assistance and analysis provided by Joel P. Schiff and Jeffrey M. Imerman and wish to thank Honey Kessler Amado for her invaluable comments.

mained on the husband as a fiduciary for his wife beyond the date of the parties' separation as to those community assets remaining in his control.⁶

*In re Marriage of Stevenot*⁷ set forth a restrictive interpretation of spousal duties. The standard of fiduciary duty, compared with a standard of "good faith" at a certain stage of the relationship, juxtaposed with a confidential relationship prior to the date of separation, created an ambiguous mix of definitions and standards. What *Stevenot* did not do was to discuss and explain the nature, scope, and meaning of the fiduciary duty between spouses before filing a dissolution proceeding.

In 1991, applicable sections of the Civil Code were amended to replace the good faith standard with a heightened duty of care between spouses, making applicable the rules governing fiduciary rela-

tionships.⁸ The ambiguity which had by then evolved, however, required definition and distinction between the standards of good faith and fiduciary duty. An attempted clarification came in 1994 in *In re Marriage of Reuling*,⁹ in which the court of appeal explained that "given a stated judicial distinction between the two standards and the subsequent change in the statutory language from 'good faith' to 'fiduciary duty,' we may reasonably infer that the Legislature intended by the 1991 amendments to replace a lesser standard with one deemed higher."¹⁰

A stricter standard of spousal fiduciary duty emerged at the dawn of the new century. *In re Marriage of Brewer & Federici*¹¹ heightened the fiduciary duty and shifted the burden of disclosure to the spouse in a superior position to obtain records or financial information from which an asset could be valued.¹²

In Re Marriage of Duffy

At the time of the 2001 decision in *In re Marriage of Duffy*, Family Code Section 721 set forth the fiduciary duties between spouses. The statute specifically excluded Probate Code Section 16040 from the definition of spousal fiduciary duties. The duty of care mandated by Section 16040 is synonymous with the level of care required by the prudent investor rule.¹³ Section 16040 requires a trustee to administer a trust with "reasonable care, skill, and caution under the circumstances then prevailing that a prudent person acting in a like capacity would use...."¹⁴

*In re Marriage of Duffy*¹⁵ reversed the trial court and held that a spouse generally is not bound by the prudent investor rule and does not owe to the other spouse the duty of care that one business partner owes to another.¹⁶ The *Duffy* facts illustrate this point and are helpful in better understanding the practical impact this case would have on the duty that spouses owe to each other. Vincent and Patricia Duffy were married in 1962. For 34 years, between 1963 and 1997, Vincent made investments in real estate, business ventures, and vacation property. The trial court found that Vincent made investments without consulting his wife or obtaining her input and failed to tell her how he was funding the investments, ignored some of her requests for financial information, and treated her in a curt and dismissive manner that had the effect of discouraging further questioning. The trial court determined that Vincent breached his fiduciary duty to his wife and ordered him to pay her approximately \$400,000 in damages.¹⁷ Vincent appealed the trial court's finding of breach of his fiduciary duty; Patricia appealed the trial court's denial of her request for fees. The Second District affirmed in part and reversed in part.

The court of appeal dealt with the degree of Patricia's requests and the degree of Vincent's refusals to respond. The appellate panel concluded that Vincent had a duty to disclose financial information, but Patricia had a corresponding duty to request information. The court determined that the trial court had erred in concluding that Vincent breached his fiduciary duty of disclosure to Patricia. According to the court of appeal, "[A] spouse generally is not bound by the prudent investor rule and does not owe to the other spouse the duty of care one business partner owes to another....To summarize, [Vincent Duffy did not owe Patricia Duffy] a duty of care in investing the community assets. Inasmuch as [he owed her] no duty of care, he cannot have breached that duty."¹⁸

The legislature reacted swiftly to the *Duffy* decision with enactment of Senate Bill 1936. Although this amendment to Family Code Section 721, which became effective January 1, 2003, consisted of only six words and four numbers,¹⁹ it has produced a torrent of debate and uncertainty. There is a good reason why so much confusion on this topic has arisen. The language of Section 721 is seemingly inconsistent with the uncodified section of the statute. For example, the leg-

islature on one hand appears to exclude the prudent investor rule by stating at the beginning of the statute:

Except as provided in Section...16047 of the *Probate Code* [which defines and embodies the prudent investor rule], in transactions between themselves, a husband and wife are subject to the general rules governing fiduciary relationships which control the actions of persons occupying confidential relations with each other.²⁰

However, just a few lines later, in the same statute, the legislature appears to include the prudent investor rule in uncodified Section 2 in stating:

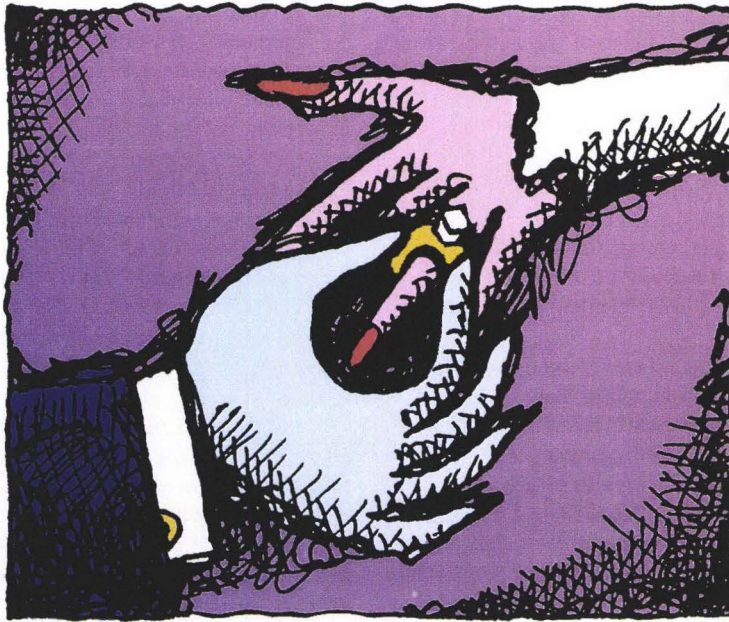
It is the intent of the Legislature in enacting this act to clarify that Section 721 of the *Family Code* provides that the fiduciary relationship between the spouses includes all of the same rights and duties in the management of community property as the rights and duties of unmarried business partners managing partnership property, as provided in Sections 16403, 16404, and 16503 of the *Corporations Code*, and to abrogate the ruling in *In re Marriage of Duffy* (2001) 91 Cal. App. 4th 923, to the extent that it is in conflict with this clarification.²¹

Many who adopt the view that the amended statute has inconsistent provisions argue that the legislature intended to exclude the prudent investor rule.²² Their argument rests on the fact that the legislature failed to specify in Section 2 of the uncodified provision which of the two holdings in *Duffy* it intended to abrogate.²³ According to this viewpoint, the legislature did not abrogate the *Duffy* holding that the prudent investor rule did not apply.²⁴ This is a legitimate argument because it attempts to harmonize the two seemingly inconsistent provisions.

A better reasoned basis for this position eliminates the fog that has hovered over the statute since its enactment. Careful reading of the cross references in Section 721 to the Probate and Corporations Codes clarifies the legislature's intent. Prior to *Duffy* and the enactment of SB 1936, the legislature excluded Probate Code Section 16040 (the duty of care contained in the prudent investor rule) from the definition of spousal fiduciary duties. With the enactment of SB 1936, the legislature also excluded Probate Code Section 16047 from the definition of spousal fiduciary duties. By excluding Section 16047 in the newly amended statute, the legislature affirmed the *Duffy* holding that spouses do not owe a duty of care to each other as non-marital business partners do.

The legislature, rather than abrogating *Duffy's* exclusion of the prudent investor rule, opted for a more moderate set of duties encompassed by amended Section 721's cross-reference to Corporations Code Section 16404.²⁵ Section 16404 requires business partners to refrain from "engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of the law."²⁶ By adding to Section

721 a reference to Corporations Code Section 16404, the legislature intended that spouses would owe each other a duty of care. However, it would be the degree of care owed between nonmarital business partners instead of the duty of care mandated by Probate Code Section 16040. For example, under Corporations Code Section 16404, a spouse's conduct would have to be more egregious to breach the fiduciary duty. Mere negligence, which would be sufficient to hold spouses accountable under Probate Code Section 16040, would not be sufficient under Corporations Code Section 16404. Thus, the legislature made



clear that spouses do indeed owe each other a duty of care, however, a lesser duty than the one rejected in *Duffy*.

This argument explains the debatable inconsistency in the provisions of Section 721. It allows *Duffy's* exclusion of the prudent investor rule to stand and clarifies which holding in *Duffy* the legislature intended to abrogate in Section 2 of the uncodified part of the statute. Meaningful support exists for the view that the prudent investor rule does not apply as part of the fiduciary duty between spouses in the new statutory language.

Although no published court of appeal case has yet dealt with these issues, two recent unpublished California appellate opinions, *In re Marriage of Fell*²⁷ and *In re Marriage of McGuire*,²⁸ share the conclusion that the prudent investor rule does not apply. In addition, well-reasoned commentary substantiates the position that the prudent investor rule does not and should not apply to the duty between spouses.²⁹

On the other hand, if one wanted to argue that the prudent investor rule does and should apply, the core argument would rest on five spe-

cific words added to Section 721. SB 1936 added the language "including, but not limited to" when referring to the duties set forth in Family Code Section 721(b)(1)-(3).³⁰ "By not limiting the right of spouses to sue each other for only the rights specifically enumerated in Family Code Section 721(b), the new code section allows spouses to sue each other for breach of fiduciary duty even though [it is] not specifically listed in Family Code Section 721(b)."³¹ If the statute expressly "excludes" the prudent investor rule, however, the general language of "including, but not limited to" does not bring it back. In statutory construction,

the specific controls over the general.³² On the other hand, the position that the fiduciary duty described in amended Section 721 is the same as contained in the prudent investor rule is strengthened in the introduction to SB 1936.³³ However, this minority viewpoint leads to numerous interpretive problems and would open the door to endless litigation.

Regardless of how one reads Section 721—to include or exclude the prudent investor rule—much can and should be done to clarify the existing law. Despite the fact that one respected family law attorney recently wrote that the new amendments "have added a welcome clarity to understanding spousal fiduciary duty,"³⁴ few would disagree that more clarity is needed. The legislature should state explicitly whether the prudent investor rule applies. It would be even more constructive if the legislature would enact language stating affirmatively what the fiduciary duty between spouses is, rather than continually obfuscating the issue with convoluted cross-references to the Family, Corporations, and Probate Codes.³⁵

The Shifting Burden of Proof

In re Marriage of Haines firmly established the doctrine in California that when one spouse alleges a breach of fiduciary duty, the burden shifts to the accused spouse to prove that he or she has not committed the breach.³⁶ There are two different theories under which courts have reached this conclusion. One theory appears in the context of undue influence and the other arises within the ambit of constructive fraud.

According to Family Code Section 721(b), transactions between a husband and a wife are subject to the general rules governing fiduciary relationships that control the actions of persons occupying confidential relations with each other. This confidential relationship imposes a duty of the highest good faith and fair dealing on each spouse, and neither shall take unfair advantage of the other.³⁷

In *Haines*, a case involving undue influence, the wife deeded her interest in a residence to her husband in exchange for his cosignature on a loan to purchase an automobile.³⁸ At the trial, the wife argued that she only deeded away her interest in the residence because of undue influence. The court held she had the burden of proving this allegation and had failed to do so.³⁹ The court of appeal reversed the trial court, observing that, although spouses have the right to enter into transactions, when an interpersonal transaction

advantages one spouse, the law presumes the transaction to have been induced by undue influence.⁴⁰

The reasoning supporting this judicially created presumption is that spouses are subject to special rules that control the actions of persons occupying confidential relations with each other.⁴¹ Because of these special rules, the burden is placed on the advantaged spouse to prove by a preponderance of the evidence that no undue influence was exerted and that the transaction was made freely and voluntarily with a complete understanding of the effect of the transfer.⁴² Based on this determination, the *Haines* court emphasized that the trial court should have placed the burden of proof on the husband, the advantaged spouse, and not on the wife.⁴³

A recent important case illuminating this principle, *In re Marriage of Delaney*,⁴⁴ held that the *Haines* presumption of undue influence overcomes the presumptions in Family Code Section 2581 (that property acquired during marriage in joint tenancy is community property) and Evidence Code Section 662 (that an owner of legal title to property owns the full beneficial title). In *Delaney*, one spouse gained an advantage over the other in a property transaction in which the husband's separate property house was transferred by grant deed to the husband and wife as joint tenants incident to obtaining a home improvement

loan. The trial court set aside the deed, and the court of appeal affirmed, relying on the *Haines* presumption of undue influence in transactions between spouses. The *Delaney* opinion restated the requisite burden to overcome the presumption of undue influence in an interspousal transaction in straightforward language that underscores the difficulty in overcoming the presumption:

[I]t was Wife's burden to establish that Husband's transmutation of the Property to joint tenancy was freely and voluntarily made, with full knowledge of all the facts, and with a complete understanding of the effect of a transfer from his unencumbered separate property interest to a joint interest as Husband and Wife.⁴⁵

One can now legitimately argue that *Delaney* has raised the bar to overcoming the *Haines* presumption of undue influence. The *Haines* standard of preponderance of the evidence to rebut the presumption remains, but *Delaney's* language and holding emphasize the strength of the presumption of undue influence and the current difficulty of overcoming it. Creative practitioners, responding to these developments, may consider addressing and attempting to overcome the presumption of undue influence in a postnuptial agreement incident to a material interspousal transfer or transmutation of property interests.

Another recent California case focusing on the burden of proof issue is *In re Marriage of Lange*.⁴⁶ *Lange* held that a rebuttable presumption arises when one spouse obtains an advantage over the other spouse in a community property transaction.⁴⁷ This result occurs because a fiduciary generally obtains an advantage if his or her position is improved, he or she obtains a favorable opportunity, or he or she otherwise gains, benefits, or profits in an interspousal transaction.⁴⁸ In *Lange*, the husband executed a promissory note and deed of trust to his wife. The court held as a matter of law that the wife received an advantage or benefit from her husband's execution of the promissory note and deed of trust because she then became a secured creditor, entitled to a 10 percent interest on her husband's obligation. As the court explained, the wife was charged with dispelling the presumption of undue influence and, because she failed to do so, the note

and the deed of trust were held unenforceable.⁴⁹

These cases are intensely fact-driven. *In re Marriage of Friedman*⁵⁰ provides a good example of a case in which a factual showing rebutted the presumption of undue influence. *Friedman* upheld a postnuptial agreement on the ground that the *Haines* presumption of undue influence was dispelled by the evidence. The husband met his burden of showing that his wife was "not induced to execute the postnuptial agreement through mistake, undue influence, fraud, misrepresentation, or any other breach of the Friedman's confidential relationship" and that there was no "taint" to the agreement.⁵¹

Burden of proof issues also arise in breach of fiduciary duty claims that involve constructive fraud. In fact, a finding of constructive fraud formed part of the basis for the holding in *Haines*. Similarly, in *In re Marriage of Baltins*, the court held that "constructive fraud comprises all acts, omissions, and concealments involving breach of legal or equitable duty, trust, or confidence, and resulting in damage to another."⁵² Numerous law review articles echo the logic and arguments of the courts.⁵³

In contrast to these cases, the court of appeal, in *Bono v. Clark*,⁵⁴ recently held that the presumption of wrongdoing does not arise simply from the disappearance of a community asset. As in cases involving undue influence, in this area of the law the inquiry is particularly fact-intensive. *Bono* upheld a trial court's determination that the wife had failed to carry her burden of proof that her husband inappropriately disposed of assets. According to this opinion, the mere absence of personal property assets years after separation is insufficient to raise an inference that the husband disposed of them inappropriately.⁵⁵

Critics of the holding in *Bono* have argued that if it can be demonstrated that certain marital assets exist on the date of separation and are in the possession of one spouse, it becomes that spouse's obligation to account for them. If he or she cannot do so, then that party should be charged for their value. To hold otherwise, opined one commentator, makes a mockery of the concept of fiduciary duty because the spouse in possession of real or personal property should bear full responsibility.⁵⁶

Potential Breaches of Fiduciary Duty

An inherent tension has long existed when one spouse chooses between separate property and community property to fund investment opportunities presented during marriage. As the duty of spouses toward each other has been heightened from disclosure to good faith and then to fiduciary duty, this tension has increased. Proposed resolution of this conflict is often addressed in prenuptial agreements. But once married, the fiduciary duty one spouse owes the other makes this tension a Hobson's choice (given the vagaries of the nature and extent of factual disclosures between married partners illustrated by *Duffy*) because of the present uncertainty in the nature and scope of spousal fiduciary duties. In *Duffy*, the court put it this way: "A breach of loyalty could occur simply from seizing an excellent investment opportunity for the benefit of one's personal property rather than for the benefit of the community estate."⁵⁷

The duty of loyalty to one's spouse and to the community has been infused into the fiduciary duty obligation.⁵⁸ If no notice is given to the other spouse and marital property is utilized for an investment, undisclosed profits are susceptible to a claim of breach of fiduciary duty, with possibly draconian results.⁵⁹ If community property is not properly handled, and the investment loses value, losses are susceptible to a claim of breach of the fiduciary duty owed to the other spouse, and a charge for the lost funds may be imposed against the mismanaging spouse.⁶⁰

A recent case illustrates the dilemma. In *In re Marriage of Destein*,⁶¹ the husband had historically successfully invested the bulk of his sep-

arate property in growth assets, specifically non-income-producing real estate. The trial court imputed investment earnings for purposes of calculating child support. On appeal, the husband contended that the trial court was not entitled to second-guess his reasonable investment strategy. The court of appeal rejected his argument and upheld the trial court's ruling. The *Destein* opinion cites case authority from other jurisdictions and text authority to support its reasoning and conclusion that the historic allocation of assets to growth, rather than income, does not preclude imputation of income to such assets.⁶² This type of second-guessing of marital investment philosophy and decision making, if applied to a prudent investor rule between spouses, could create endless litigation between spouses and requires courts to act as investment advisers.

Another recent appellate decision, *In re Marriage of Hixson*, restricted the requirement for disclosing and sharing business opportunities that are presented to just one spouse.⁶³ The trial court held that the ex-husband was not required to share a postjudgment investment opportunity with his ex-wife because, based on Family Code Section 2102(a), the asset had been distributed by a stipulated judgment.⁶⁴ However, there was no indication in the opinion that the asset had "actually been distributed" as required by Section 2102(b), and continuation of the fiduciary duty until distribution, as required by that section, should have been discussed and considered.⁶⁵ The surprisingly restrictive opinion in the *Hixson* case teaches the lesson that duration of the spousal fiduciary duties after separation and even judgment

must be carefully examined under both Family Code Section 2102(a) and Section 2102(b).

It is difficult enough in California for intended spouses to negotiate and sign an enforceable prenuptial agreement. Statistics tell us it is even harder to stay married. Now we see that even during marriage, California spouses are confronted with a combustible mix of disclosures, decisions, and duties that affect their money, investments, businesses, and financial well-being. Ultimately, their emotional well-being is at stake when the complexities of legislative enactments and judicial interpretation are made known to them. Professional representatives, including attorneys, accountants, business managers, investment advisers, and financial planners have a duty and responsibility to inform clients of their rights and responsibilities during all stages of a relationship. It is no longer acceptable to wait until things go wrong, to advise clients after the fact of the new rules and standards. As the court of appeal recently observed: "Judicial decisions in family law cases have lasting effects on the parties' homes, familial relationships, and families."⁶⁶ The new rules and standards, amended statute, spirited current debate, and changing and often inconsistent judicial interpretations are too critically important to overlook when providing advice to clients. Professional excellence and responsibility to clients deserve no less commitment than faithful and continuing study and critique of this evolving and important area of the law. ■

¹ *Vai v. Bank of Am.*, 56 Cal. 2d 329, 15 Cal. Rptr. 71 (1961).

² *Bank of Calif. v. Connolly*, 23 Cal. 3d 590, 600, 153 Cal. Rptr. 423 (1973).

³ *Id.*

⁴ *Id.*

⁵ *Id.*

⁶ *In re Marriage of Munguia*, 146 Cal. App. 3d 853, 195 Cal. Rptr. 199 (1983).

⁷ *In re Marriage Stevenot*, 154 Cal. App. 3d 151, 202 Cal. Rptr. 116 (1984).

⁸ CIV. CODE §§5103, 5125, 5125.1.

⁹ *In re Marriage of Reuling*, 23 Cal. App. 4th 1428, 28 Cal. Rptr. 2d 726 (1994).

¹⁰ *Id.*

¹¹ *In re Marriage of Brewer & Federici*, 93 Cal. App. 4th 1334, 113 Cal. Rptr. 2d 849 (2001).

¹² *Id.*

¹³ PROB. CODE §§16045-16054. Probate Code §16040 mandates the same standard of behavior as the prudent investor rule, but is not called the "prudent investor rule" and falls outside the Uniform Prudent Investor Act.

¹⁴ PROB. CODE §16040.

¹⁵ *In re Marriage of Duffy*, 91 Cal. App. 4th 923, 111 Cal. Rptr. 2d 160 (2001).

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.* The *Duffy* court's reference to a duty of care is the equivalent of the prudent investor rule.

¹⁹ FAM. CODE §721(b) (amended effective Jan. 1, 2003). The following is the text of the prior version of Family

Code §721 indicating changes enacted by SB 1936:

§ 721 Contracts with each other and third parties; fiduciary relationship

(a) Subject to subdivision (b), either husband or wife may enter into any transaction with the other, or with any other person, respecting property, which either might if unmarried.

(b) Except as provided in Sections 143, 144, 146, and 16040 and 16047 of the Probate Code, in transactions between themselves, a husband and wife are subject to the general rules governing fiduciary relationships which control the actions of persons occupying confidential relations with each other. This confidential relationship imposes a duty of the highest good faith and fair dealing on each spouse, and neither shall take any unfair advantage of the other. This confidential relationship is a fiduciary relationship subject to the same rights and duties of nonmarital business partners, as provided in Sections ~~15010, 15020, 15021, and 15022~~ 16403, 16404, and 16503 of the Corporations Code, including, but not limited to the following:

(1) Providing each spouse access at all times to any books kept regarding a transaction for the purposes of inspection and copying.

(2) Rendering upon request, true and full information of all things affecting any transaction which concerns the community property. Nothing in this section is intended to impose a duty for either spouse to keep detailed books and records of community property transactions.

(3) Accounting to the spouse, and holding as a trustee, any benefit or profit derived from any transaction by one spouse without the consent of the other spouse which concerns the community property.

Sec. 2: It is the intent of the Legislature in enacting this act to clarify that Section 721 of the Family Code provides that the fiduciary relationship between the spouses includes all of the same rights and duties in the management of community property as the rights and duties of unmarried business partners managing partnership property, as provided in Sections 16403, 16404, and 16503 of the Corporations Code, and to abrogate the ruling in *In re Marriage of Duffy* (2001) 91 Cal. App. 4th 923, to the extent that it is in conflict with this clarification.

²⁰ *Id.*

²¹ *Id.*

²² Garrett C. Dailey, *Fiduciary Duty and the Prudent Investor Rule: Legislature Continues Efforts to Define Marital Duties*, ATTORNEY'S BRIEFCASE 94-97 (2003); Garrett C. Dailey, *Prudent Investor Rule Does Not Apply to Investment Decisions Made During Marriage—Yet*, FAMILY L. NEWS, Summer 2003, at 5-6.

²³ *Id.*

²⁴ *Id.*

²⁵ *Id.*

²⁶ CORP. CODE §16404

²⁷ *In re Marriage of Fell*, 2003 WL 21380860 (Cal. App. 2d Dist., June 16, 2003) (unpublished).

²⁸ *In re Marriage of McGuire*, 2002 WL 177279 (Cal. App. 2d Dist., Aug. 1, 2002) (unpublished) (decided prior to Jan. 1, 2003, the date the amendment to FAM. CODE §721 became effective.)

²⁹ Dailey, *supra* note 22.

³⁰ Peter M. Walzer & Gregory W. Herring, *What Words Don't You Understand—Fiduciary or Duty? In Amending Family Code Section 721, the Legislature Gives Unhappy Couples One More Thing to Fight About*, FAM. L. NEWS,

Winter 2003, at 5-7.

³¹ *Id.*

³² CODE CIV. PROC. §1859.

³³ The introduction states: "[T]his bill would subject a husband or wife that enters into any real property transaction with the other to those general rules governing fiduciary relationships where the transaction involves the administering of a trust." Unfortunately, this explanatory language is confusing. The reference to only real property makes no sense, inasmuch as Section 721 otherwise expressly applies to all property transactions. Nonetheless, this language undeniably expresses an intent to apply the prudent investor rule to marital transactions.

³⁴ Diana Richmond, *Clarifying the Marital Partnership*, CAL. FAM. L. MONTHLY, Feb. 2003, at 43-46.

³⁵ See FAM. CODE §721; PROB. CODE §§143, 144, 146, 16040, 16047; and CORP. CODE §§16403, 16404, 16503.

³⁶ *In re Marriage of Haines*, 33 Cal. App. 4th 277, 39 Cal. Rptr. 2d 673 (1995).

³⁷ FAM. CODE §721(b).

³⁸ *Haines*, 33 Cal. App. 4th at 284.

³⁹ *Id.* at 297.

⁴⁰ *Id.* at 293.

⁴¹ *Id.*

⁴² *Id.* at 295-297; HOGOBOOM & KING, CALIFORNIA PRACTICE GUIDE TO FAMILY LAW Ch. 8-B at 559-74 (2002).

⁴³ *Haines*, 33 Cal. App. 4th at 297.

⁴⁴ *In re Marriage of Delaney*, 111 Cal. App. 4th 991, 4 Cal. Rptr. 3d 378 (2003).

⁴⁵ *Id.* at 999-1000.

⁴⁶ *In re Marriage of Lange*, 102 Cal. App. 4th 360, 125 Cal. Rptr. 2d 379 (2002).

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *In re Marriage of Friedman*, 100 Cal. App. 4th 65, 122 Cal. Rptr. 2d 412 (2002).

⁵¹ *Id.*

⁵² *In re Marriage of Baltins*, 212 Cal. App. 3d 66, 260 Cal. Rptr. 403 (1989). See also *Estate of Cover*, 188 Cal. 133 (1922).

⁵³ Bradley L. Adams, *The Doctrine of Fraud on the Community*, 49 BAYLOR L. REV. 445 (1997); Alexandria Streich, *Spousal Fiduciaries in the Marital Partnership: Marriage Means Business but the Sharks Do Not Have a Code of Conduct*, 34 IDAHO L. REV. 367 (1997). Both law review articles support the argument that the presumption of constructive fraud shifts the burden of proof.

⁵⁴ *Bono v. Clark*, 103 Cal. App. 4th 1409, 128 Cal. Rptr. 2d 31 (2002), *rev. denied*.

⁵⁵ *Id.*

⁵⁶ Dailey, *supra* note 22.

⁵⁷ *In re Marriage of Duffy*, 91 Cal. App. 4th 923, 937, 111 Cal. Rptr. 2d 160 (2001).

⁵⁸ Richmond, *supra* note 34.

⁵⁹ *In re Marriage of Rossi*, 90 Cal. App. 4th 34, 108 Cal. Rptr. 2d 270 (2001).

⁶⁰ *In re Marriage of Hokanson*, 68 Cal. App. 4th 987, 80 Cal. Rptr. 2d 699 (1998).

⁶¹ *In re Marriage of Destein*, 91 Cal. App. 4th 1385, 111 Cal. Rptr. 2d 487 (2001).

⁶² *Id.* at 1394-96.

⁶³ *In re Marriage of Hixson*, 111 Cal. App. 4th 1116, 4 Cal. Rptr. 3d 483 (2003), *reh'g denied, petition for rev. filed* (Nov. 4, 2003).

⁶⁴ *Id.*; FAM. CODE §2102(a).

⁶⁵ Hixson, 111 Cal. App. 4th 1116; FAM. CODE §2102(b).

⁶⁶ *Settlemyre v. Superior Court*, 103 Cal. App. 4th 1150, 127 Cal. Rptr. 2d 381 (2002); JUDICIAL COUNCIL OF CALIFORNIA, ADMINISTRATIVE OFFICE OF COURTS, REPORT OF THE SUBORDINATE JUDICIAL OFFICER WORKING GROUP ON SUBORDINATE JUDICIAL OFFICERS DUTIES AND TITLES 22 (2002).

November 2014
Volume 2014 • Issue No. 11

GUEST ARTICLE

*Marshall S. Zolla, Esq.**

The California Lawyer's Grey Fog of Uncertainty: Assessing a Client's Diminished Mental Capacity

Portions of this article were derived from The California Lawyer's Grey Fog of Uncertainty: Assessing a Client's Diminished Mental Capacity, copyright 2012, Regents of the University of California. Those portions are reprinted with permission of the Regents of the University of California.

As our population ages¹ and the number of Americans with Alzheimer's disease grows,² an increasingly

*Mr. Zolla is a Certified Family Law Specialist who practices in Los Angeles. Mr. Zolla has been a contributor and member of the Editorial Board of the California Family Law Monthly for the past 26 years. He is a Fellow of the American Academy of Matrimonial Lawyers. Mr. Zolla concentrates his firm's practice in the full range of complex and sophisticated family law issues, and the firm's clients include professionals, business executives and prominent persons in the fields of politics, sports and entertainment.

¹ California is projected to be one of the fastest growing States in the nation in total population. In 1990, California comprised 12 percent of the nation's population and is expected to have 14 percent of the nation's population by 2020. In California, the elderly population is expected to grow more than twice as fast as the total population and this growth will vary by region. The elderly age group will have an overall increase of 112 percent during the period from 1990 to 2020. More than half the counties will have over a 100 percent increase in this age group. The influence of the 60 and over age group on California is expected to emerge most strongly between 2000 to 2020. Journal of the Center for Families, Children and the Courts [6 J. Center for Families, Child. & Cts. 73 (2005)]; www.aging.ca.gov.

² An estimated 5.2 million Americans age 65 and older (approximately one in nine) currently have Alzheimer's disease, and the number is projected to reach 8.4 million by 2030. Alzheimer's Association, 2014 Alzheimer's Disease Facts and Figures, Alzheimer's & Dementia, Volume 10, Issue 2, pp. 16, 21 www.alz.org/downloads/Facts_Figures_2014.pdf.

frequent decision is faced by California attorneys: What ethical rules govern a California attorney's assessment of a client's suspected diminished mental capacity? This determination becomes crucial in family law matters, where sensitive issues involving finances, real estate, children, grandchildren, beneficiary designations, estate planning and retirement benefits all require the informed consent of a competent client. A California attorney cannot currently seek outside expert advice to assess a client's suspected diminished capacity without the client's consent. Doing so violates the strict duty of confidentiality owed to the client. There is a current evolving shift away from this restrictive policy, but it has not yet been officially adopted by the legislature, the state bar or the Supreme Court. Counsel must therefore proceed with caution, bearing in mind the guidelines set forth in the Due Process in Competence Determinations Act [Probate Code §§ 810-813]. If a client lacks capacity, counsel should consider withdrawing from the representation. If counsel believes the client has sufficient capacity, but thinks there might be a challenge to the client's capacity later on, counsel should document in detail the client's indicia of capacity with meticulous notes.

The American Bar Association (ABA) Model Rules of Professional Conduct, Rule 1.14, permit counsel to consult with third parties to determine client capacity. California law is more stringent. Under the California view, the duty of client confidentiality is paramount and prevents counsel from consulting third parties and divulging client confidences to determine client capacity. There thus exists a conflict between the ABA Model Rules of Professional Conduct, Rule 1.14, and California law as set forth in *Business and Professions Code* Section 6068(e).

ABA Model Rule 1.14

(a) When a client's capacity to make adequately considered decisions in connection with a representation is diminished, whether because of minority, mental impairment or for some other reason, the lawyer shall, as far as reasonably possible, maintain a normal client-lawyer relationship with the client.

(b) When the lawyer reasonably believes that the client has diminished capacity, is at risk of substantial physical, financial or other harm unless action is

taken and cannot adequately act in the client's own interest, the lawyer may take reasonably necessary protective action, including consulting with individuals or entities that have the ability to take action to protect the client and, in appropriate cases, seeking the appointment of a guardian ad litem, conservator or guardian.

(c) Information relating to the representation of a client with diminished capacity is protected by Rule 1.6³. When taking protective action pursuant to paragraph (b), the lawyer is impliedly authorized under Rule 1.6(a) to reveal the information about the client, but only to the extent necessary to protect the client's interests. (Emphasis added.)

ABA Rule 1.14(b) suggests that it would be ethical for counsel to take reasonably necessary protective action, such as consulting with third parties to assess a client, where counsel believes capacity is an issue.

California Business and Professions Code Section 6068(e)

Business and Professions Code Section 6068(e) embraces a broad duty of confidentiality which prohibits disclosure by counsel of any client information learned in the course of the attorney-client relationship. The statutory exception is where the attorney believes disclosure is necessary to prevent a criminal act reasonably believed likely to result in an individual's death or substantial bodily harm.

In 1989, the Standing Committee on Professional Responsibility and Conduct of the State Bar of California issued Ethics Opinion No. 1989-112, addressing whether counsel may institute conservatorship proceedings for a client without the client's consent, where counsel concludes the client is incompetent to act in his/her best interest. That opinion concluded that it is unethical for an attorney to institute conservatorship proceedings contrary to the client's wishes, as doing so requires the attorney to divulge client secrets and represent either conflicting or adverse interests. Under the California view,

³ ABA Model Rule 1.6(a) provides that "A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted by paragraph (b)."

instituting such a proceeding for a client without capacity violates California Rules of Professional Responsibility, Rule 3-310, in which counsel cannot represent conflicting interests, absent the informed written consent of all parties concerned.

Ethics Opinion 1989-112 is still viewed as a valid ethical guideline. A current practice guide warns counsel not to institute proceedings for appointment of a conservator even where an attorney recognizes his/her client may need one:

[Ethics Opinion 1989-112] ruled that an attorney who petitions for a conservatorship for his or her client without the client's consent violates the attorney's duties to protect client secrets and to avoid conflicts of interest. . . . The exceptional situation would occur if the client consented to the attorneys' petition while the client still had capacity. Very few attorneys seek such consent from their clients and thus, as a general rule, attorneys may not petition to have a conservator appointed for a client.

[*California Conservatorship Practice* (CEB June 2011) § 1.6, p. 9-10].

California Conservatorship Practice also acknowledges the existence of objections to Ethics Opinion 1989-112 and a growing trend to change direction on this issue to side with ABA Model Rule 1.14(b). For example, the Estate Planning, Trust and Probate Law Section of the State Bar was troubled by the subject Ethics Opinion, and urged that California adopt a Rule of Professional Conduct similar to ABA Model Rule 1.14. The Legal Ethics Committee of the Bar Association of San Francisco also disagreed with the ethics opinion and concluded that "counsel who reasonably believes that a client is substantially unable to manage his or her own financial resources or to resist fraud or undue influence may, but need not, take protective action with respect to the client's person or property." (*Id.*)

In 2010 the State Bar Board of Governors considered a new proposed rule which largely mirrored ABA Model Rule 1.14, except that it specified that counsel could not file or represent a person filing a conservatorship proceeding. Earlier, in 2005, the Executive Committee of the Trusts and Estates Section of the State Bar of California proposed adding *Business and Professions Code* Section

6068.5, to allow an attorney to make limited disclosures about a client to one who has the ability to take action to protect the client. That proposed statute would have created an exception to *Business and Professions Code* Section 6068(e), which imposes the attorney-client duty of loyalty and confidentiality, and would have allowed disclosure only if the client's decision-making capacity was sufficiently impaired to support an incapacity determination under *Probate Code* Section 811 and the client was at risk of substantial physical, financial, or other harm. Like the proposed rule, the proposed statute virtually mirrored ABA Model Rule 1.14, but prohibited counsel from filing a petition for conservatorship for the impaired client. As of this date, the proposed rule has not been adopted, nor has specific legislation been introduced to address or resolve this issue.

For now, Ethics Opinion 1989-112 remains valid. California attorneys cannot divulge client confidences for the purpose of obtaining assistance in determining client capacity.

California Case Law

Andersen v. Hunt (2011) 196 Cal.App.4th 722 is instructive in determining the different legal standards that apply when deciding whether or not a person has the mental capacity to execute a will or a trust. **The Court of Appeal held where a person simply amends a trust, that person's capacity should be determined by the lower standard of executing a will, which is set forth in *Probate Code* Section 6100.5.**

In that case, Wayne Andersen and his wife established a family trust in 1992, which left all of their assets to their two children. In 2003, ten years after his wife died, Wayne suffered a stroke, following which he amended the trust to leave 60% of the assets to his long-time partner and caretaker, Pauline Hunt. The remaining 40% was split equally among his two children and his grandson. The trial court ruled that Wayne did not have the requisite contractual capacity to execute the trust amendments. In doing so, the trial court held Wayne to the higher standard of contractual capacity set forth in *Probate Code* Section 811 and 812, rather than the lower standard of testamentary capacity set forth in *Probate Code* Section 6100.5.

The Court of Appeal held that the trial court erred when it evaluated Wayne's capacity to execute the trust amendments by applying the higher standard of mental capacity set forth in *Probate Code* Sections 810-812 ("contractual capacity") rather than the lower standard applicable to "testamentary capacity" codified in *Probate Code* Section 6100.5. The court stated that "[w]hen determining whether a trustor had capacity to execute a trust amendment that, in its content and complexity, closely resembles a will or codicil, we believe it is appropriate to look to section 6100.5 to determine when a person's mental deficits are sufficient to allow a court to conclude that the person lacks the ability 'to understand and appreciate the consequences of his or her actions with regard to the type of act or decision in question.' (§ 811, subd. (b).) In other words, while section 6100.5 is not directly applicable to determine competency to make or amend a trust, it is made applicable through section 811 to trusts or trust amendments that are analogous to wills or codicils." As a result, the Court of Appeal found that when Wayne's capacity was evaluated under the correct lower standard, there was no substantial evidence that Wayne lacked capacity to execute the 2003 and 2004 trust amendments.

The Court of Appeal based its holding on well-established law in California that a testator is presumed competent and the burden rests on the person challenging competency to overcome the presumption. A person lacks capacity to make a will if, at the time of the making of the will, he or she cannot understand the nature of the testamentary act, recall the nature of his or her assets, or recall his or her relations to living descendants and those whose interests are affected by the will. In the unpublished portion of the opinion, the Court of Appeal concluded that there was no substantial evidence that Wayne lacked testamentary capacity to execute the trust amendments.

Moore v. Anderson Zeigler Disharoon Gallagher & Gray, P.C. (2003) 109 Cal.App.4th 1287 also provides insight into the issue of counsel's obligation to determine a client's testamentary capacity in the course of representation. In that case, the testator's children filed a legal malpractice lawsuit against the attorney who prepared the testator's will, alleging that the attorney should have recognized that the

client did not have testamentary capacity to change his estate planning documents. The trial court sustained the attorneys' demurrer without leave to amend and the children appealed. The Court of Appeal affirmed, holding that an attorney preparing a will for a client does not owe a duty to non-client beneficiaries to ascertain and document the client's testamentary capacity. To hold otherwise could compromise the attorney's duty of loyalty to the client and also, perhaps, put the attorney in the position of potentially conflicting duties to different beneficiaries [*Id.*].

Although *Moore* addressed the capacity issue in the context of non-client beneficiaries, in dicta, the Court of Appeal acknowledged California's heightened policy regarding the duty of loyalty to a client. The Court of Appeal advised that prudent counsel should be familiar with the test for capacity set forth in *Probate Code* Section 811 *et seq.*; however, "in accordance with case law, . . . because the attorney owes his or her undivided loyalty to the interests of the client, the attorney's only duty of care is to intended beneficiaries of a testator client whose testamentary rights are impaired by negligent drafting. (Citation omitted.) So paramount is the duty of loyalty, that in this state, the attorney may not institute conservatorship proceedings on a client's behalf without consent, even when the attorney concludes the client is incompetent, because of the prohibition against disclosure of client confidences" [*Id.* at 1306 – 1307 (emphasis added)].

In *Moore*, the children-appellants argued on appeal that competent counsel has a duty to his/her testator client to ascertain the client's competence before drafting a will and to document that exploration. The Court of Appeal disagreed, acknowledging the pitfalls inherent in requiring counsel to determine testator capacity:

It may be that prudent counsel should refrain from drafting a will for a client the attorney reasonably believes lacks testamentary capacity or should take steps to preserve evidence regarding the client's capacity in a borderline case. However, that is a far cry from imposing malpractice liability to nonclient potential beneficiaries for the attorney's alleged inadequate investigation or evaluation of capacity or the failure to sufficiently document that

investigation. None of the cited secondary sources appear to even suggest imposition on the attorney of such a duty to nonclient. We conclude that the policy considerations present in these circumstances and discussed above strongly militate against imposition on the testator's lawyer of a duty to nonclient beneficiaries to investigate, evaluate and ascertain the testator's capacity or to document the same.

[*Id.* at 1305 – 1307].

Moore is instructive because it provides guidance in dealing with clients who may lack legal capacity. The *Moore* court suggests that prudent counsel should refrain from engaging in work for a client where counsel reasonably believes the client lacks capacity. In a borderline case, counsel should preserve evidence regarding the client's capacity. This approach is also suggested in the article mentioned below.

In *In re Marriage of Greenway* (2013) 217 Cal. App. 4th 628, the 76-year-old husband, Lyle, sought to end his marriage to Joanne, his wife of 48 years. The trial court rejected Joanne's argument that Lyle was mentally incompetent and incapable of making a reasoned decision regarding his marital status, and granted his request for a status-only dissolution. In affirming, the Court of Appeal determined that the mental capacity required to end one's marriage is similar to the mental capacity required to enter into the marriage, i.e., the baseline presumption of mental capacity is based upon the criteria set forth in *Probate Code* section 811 (part of the Due Process in Competence Determinations Act). As framed by the appellate opinion, notwithstanding the fact that the testifying experts agreed that Lyle had dementia, the question was whether his impairment was such that he no longer had the capacity of making a reasoned decision to end his marriage. In analyzing conflicting arguments, the Court of Appeal determined that a person's mental capacity is fact specific, and the level of required mental capacity changes depending on the issue at hand. The *Greenway* court concluded that mental capacity can be measured on a sliding scale, with marital capacity requiring the least amount of capacity, followed up the scale by testamentary capacity, and, on the high end of the scale, the mental capacity required to enter into contracts.

Likewise, according to the *Greenway* court, the burden of proof with respect to mental capacity

changes depending on the issue presented. There exists a presumption in favor of a person seeking to marry or make a will, but not a person executing a contract. In its summary of overlapping statutes with varying semantics relating to mental capacity, the court held that the required level of understanding rests entirely on the complexity of the decision being made: case authority evidences an extremely low level of mental capacity needed before the decision to marry or to execute a will. Similarly, the standard for testamentary capacity is also relatively low. However, the capacity to contract, which includes the capacity to convey, create a trust, make gifts and to grant powers of attorney, requires the baseline criteria contained in *Probate Code* sections 811 and 812, as well as the specific guidelines for determining the capacity to contract embraced in *Civil Code* section 39(b).

Finally, in *Lintz v. Lintz* (2014) 222 Cal.App.4th 1346, the court set aside a transmutation of separate property to community property, as well as provisions for a spouse under a living trust. The court held that *Family Code* Section 721 imposes a fiduciary duty between spouses, and the probate Court should have applied a presumption of undue influence. The court also held that the Probate Court should have applied a “sliding scale” standard of contractual capacity (based on the complexity of the documents) under *Probate Code* Sections 810 to 812, rather than the testamentary capacity standard of *Probate Code* Section 6100.5.

Mind Over Matters: The Question of an Elder’s Legal Capacity Nearly Always Involves Issues of Fraud and Undue Influence

In October 2007, Los Angeles Lawyer published an article, *Mind Over Matters: The Question of an Elder’s Legal Capacity Nearly Always Involves Issues of Fraud and Undue Influence*, by Sherrill Y. Tanibata. The article addresses counsel’s determination of client capacity and balancing the duties of loyalty and confidentiality. Tanibata contends that counsel is required, both practically and ethically, to resolve critical questions of client capacity (e.g., does the client have capacity, if not, how much is diminished, etc.). Basic guidelines and definitions for capacity are set forth in both the *Civil Code* and

the *Probate Code* [*Probate Code* §§ 810-813, 1801, 1881, 3201, 3204], pursuant to the Due Process in Competence Determinations Act [Tanibata, *Mind Over Matters: The Question of an Elder’s Legal Capacity Nearly Always Involves Issues of Fraud and Undue Influence* (Oct. 2007) 30 L.A. Law. 28].

The article cites the current conflict set forth above between California *Business and Professions Code* Section 6068(e) and the American Bar Association, Model Rules of Professional Conduct, Model Rule 1.14. California strictly construes counsel’s duty of loyalty and confidentiality to a client, without making any special provision for one with diminished capacity, versus the flexible standard afforded by the ABA. California’s “duty of loyalty strictly prohibits an attorney from initiation of conservatorship proceedings regarding a client with diminished capacity without the client’s consent. The duty of confidentiality constrains an attorney from disclosing confidential information to individuals, institutions, agencies, and even family members who might help a client with diminished capacity.” (*Id.* at 30.) The ABA model rule was adopted by a majority of states, but not California; in fact, the ABA model rule was expressly rejected by the State Bar of California’s Formal Ethics Opinion No. 89-112.

Beginning in 2004, the State Bar proposed adopting a rule similar to the ABA Model Rule, which effort was coupled with a proposal for a new *Business and Professions Code* Section 6068.5 “that would not only codify the new rule but also thereby create exceptions to *Business and Professions Code* Section 6068(e)’s duty for attorneys to ‘maintain inviolate the confidence and preserve the secrets of [the] client’ ” [*Id.* at 31]. Ultimately, neither of these efforts was successful. According to Tanibata, “the new rule, and proposed legislation if enacted, [would have relieved] the attorney to some extent from the conflict that naturally arises from the duties of loyalty and confidentiality to the client and the duty to question and assess the capacity of the client.”

Tanibata offers the following advice to counsel in how to govern their relationship with clients suffering from suspected diminished capacity:

[P]ractitioners confronted with a client whose capacity is questionable or whose capacity could be subject to question in the future must assume that they will be held to the strictest

duty to represent the client's interest even when that interest diverges from what practitioners believe to be the client's best interest. Thus, if an attorney makes an initial determination that the client lacks capacity to engage in the transaction for which the client consulted with the attorney, then the attorney must decline to act and permit the client to seek other representation. The attorney may make a recommendation to the client for a conservatorship, always subject to the caveat that an attorney may not initiate conservatorship proceedings without the client's consent (Moore v. Anderson Zeigler Disharoon Gallagher & Gray, P.C., (2003) 109 Cal. App. 4th 1287, 1306.)...

In the course of representation, counsel should reasonably assess a client's capacity using common sense and the guidelines set forth in the Due Process in Competence Determinations Act (*Probate Code* §§ 810-813, 1801, 1881, 3201, 3204). *Probate Code* Section 811 sets forth criteria in determining an "unsound mind;" *Probate Code* Section 812 sets forth criteria in determining "capacity to make a decision;" and *Probate Code* Section 6100.5 sets forth the criteria to determine "testamentary capacity." As noted above in *Andersen*, the standards are not the same. If counsel believes a client suffers from diminished capacity, counsel cannot at this time initiate a conservatorship proceeding for the client without the client's consent. Nor can counsel divulge client confidences to third persons.

If counsel believes the client lacks capacity, it would be prudent to document the client's capacity in the course of the client's representation. As suggested by *Moore*, counsel might document a client's present mental and physical state and keep detailed notes of the client's communications, disposition, and behavior in the client intake interview and during the course of representation. Perhaps a memorandum to the file would assist in establishing client capacity if subsequent litigation ensues on that issue. If counsel suspects that other parties might attack the validity of an instrument or legal document, counsel might consider retaining an expert psychiatric consultant to affirm the client's capacity; or the client can be videotaped when signing a

document in which the client states she/he fully understands the nature of the legal agreement or instrument upon executing it. Counsel should be careful, though, because retaining a consultant can backfire with a potentially discoverable report that the client does in fact lack capacity.

Counsel must proceed with caution in handling the issue of suspected diminished capacity, adhering to the client's best interest, which may not be consistent with what counsel personally believes is the client's best interest under the current state of California law and the existing Rules of Professional Conduct.

June 2012
Volume 2012 • Issue No. 06

Mediation Confidentiality vs. Breach of Spousal Fiduciary Duty: The Clash of Enshrined Public Policy Titans

By Marshall S. Zolla, Esq.;
Deborah Elizabeth Zolla, Esq.; Vivian Carrasco Hosp, Esq.*

Many of us grew up hearing the equation $E=mc^2$, without really knowing what it meant.¹ $MC=FD^2$ [Mediation Confidentiality = Fiduciary Duty (Squared)] is the new physics of family law. This equation now forms the energy content of many family law cases because of the potential clashes between competing public policies.

Both the doctrine of mediation confidentiality and the mandate of spousal fiduciary duty are well enshrined in California law. They are both core fundamental principles that have evolved and expanded significantly over the past decade. They are both policies that courts seek to protect and preserve, and both are held in the highest judicial regard. But what happens when these two public policies clash? Which policy should prevail—the steel curtain of mediation confidentiality, or the sanctified public policy of spousal fiduciary duty?

Copyright ©2012, Marshall S. Zolla, Deborah Elizabeth Zolla and Vivian Carrasco Hosp. All rights reserved. Reprinted with permission.

* Mr. Zolla is a Certified Family Law Specialist who practices in Century City. Mr. Zolla has been a contributor and member of the editorial board of the California Family Law Monthly for the past 24 years. Deborah Elizabeth Zolla and Vivian Carrasco Hosp are associates with the Law Offices of Marshall S. Zolla and concentrate their practice on complex family law matters, including prenuptial agreements, postnuptial agreements and sophisticated issues in marital dissolution proceedings.

The only published case in the family law context that deals with this conflict is *In re Marriage of Kieturakis*.² That case, as explained more thoroughly below, holds that when the two competing policies collide, mediation confidentiality prevails. *Rinaker v. Superior Court*³ and *Olam v. Congress Mortgage Co.*,⁴ both non-family law cases, reach a different conclusion by creating judicial exceptions to strict mediation confidentiality. Both cases employ a balancing test to weigh the competing policies and both arguably remain good law.⁵ Which doctrine will prevail in any given factual context remains unclear, but it is critical for family law practitioners to be aware of the potential conflict.

Consider, for example, the way these principles may clash when a couple retains a mediator to help negotiate and draft a postnuptial agreement. In our hypothetical case, Brad asks Linda to sign a postnuptial agreement a month after they are married. The agreement is then negotiated and drafted with the help of a neutral mediator. Because they are husband and wife, each owes the other a fiduciary duty to disclose all assets and liabilities and all material facts regarding valuation of assets and liabilities, income and expenses. Years later, the parties separate. Linda discovers that Brad withheld material information during the negotiation—that merger talks regarding his business were taking place during preparation of the postnuptial agreement. The merger was later consummated, and had a material impact on the valuation of Brad's company. Linda contends that by failing to disclose the merger negotiations during preparation of their agreement, Brad breached his spousal fiduciary duty to her under Family Code Section 721.⁶ In response, Brad maintains that any evidence he might present to defend against Linda's claim would directly invade mediation confidentiality. As a result, he contends, any information discussed, negotiated and exchanged is precluded under the doctrine of mediation confidentiality.

Both Linda and Brad are correct. Brad should have disclosed the merger talks and had a duty to do so under California law. But is he “off the hook” and can he escape liability because they went to a mediator to draft the agreement? If the answer is yes, then future parties in Brad’s position will seek to mediate such agreements, knowing they will be fully protected regardless of any misrepresentations or breaches of fiduciary duty. If the answer is no, then full disclosure becomes more important than mediation confidentiality, and a person in Brad’s position will not be able to use mediation confidentiality as a protective shield. The answer to this question is not yet clear, even after *Kieturakis*, but it is essential for practitioners to keep this issue in mind and to be aware of the possible arguments and contentions on both sides.

I. THE BLACK BOX OF MEDIATION CONFIDENTIALITY

The Ninth Circuit Court of Appeals recently reaffirmed the policy of mediation confidentiality with its ruling in *Facebook, Inc. v. Pacific Northwest Software, Inc.*⁷ The facts of the case were famously portrayed in the film, *The Social Network*. Cameron Winklevoss, Tyler Winklevoss, and Divya Narendra sued Facebook and Mark Zuckerberg in Massachusetts, claiming that Zuckerberg stole the idea for Facebook from them. Facebook countersued in federal court in California. The federal court ordered the parties to mediate.

After a day of mediation, the Winklevosses, their competing social networking company (ConnectU), and Facebook entered into a written settlement agreement in which the Winklevosses agreed to give up ConnectU in exchange for cash and stock in Facebook. The parties stipulated that the agreement was confidential and binding, and could be submitted into evidence only for purposes of enforcement. The settlement fell apart during negotiations over the content of the final documents, and Facebook filed a motion to enforce the agreement. The district court held that the mediated agreement was enforceable.

The Winklevosses appealed, arguing, among other things, that Facebook misled them to believe its shares were worth four times their actual value. If they had known this at the time of the mediation, they contended, they would have never signed the settlement agreement. In support of their claims, the Winklevosses presented evidence of what was said during the mediation. The Ninth Circuit agreed with the district court’s decision to exclude the evidence, albeit for different reasons. The district court relied on a local ADR rule which protected

mediation confidentiality. The Ninth Circuit, on the other hand, relied on a clause in the mediation agreement itself, which expressly provided that all statements made during the course of mediation were privileged, and could not be introduced as evidence in any judicial or other proceeding. The clause precluded the Winklevosses from introducing any evidence of what Facebook said, or did not say, during the mediation. Thus, the plaintiffs could not establish that Facebook misled them as to the value of its shares, and their claims failed. In spite of Facebook’s alleged fraud, the Court of Appeal relied upon and upheld the policy of mediation confidentiality. The Ninth Circuit found no basis for allowing the Winklevosses to back out of a deal that appeared favorable in light of subsequent market activity, a deal they reached with the help of a team of lawyers and a financial advisor.⁸

Another recent major mediation confidentiality case is *Cassel v. Superior Court*,⁹ in which the California Supreme Court continued its strict adherence to the doctrine that mediation confidentiality has no exceptions, absent an express waiver. In *Cassel*, the petitioner-client filed a complaint against his former attorneys, alleging that they had breached their professional duty by providing improper advice during mediation in order to force him to settle his case. The petitioner wanted to use conversations he had with his attorneys preceding and during the mediation to establish his case. The trial court ruled that discussions between the client and his attorneys prior to and during mediation were inadmissible. The Court of Appeal reversed, reasoning that the mediation confidentiality statutes were not intended to prevent a client from using communications with his or her attorney outside the presence of other mediation participants in a legal malpractice case against the attorney.

Relying on its past decisions,¹⁰ the California Supreme Court reversed, strictly construing the mediation confidentiality statute, Evidence Code § 1119, to hold that the petitioner’s discussions with his attorneys before and during the mediation were protected by mediation confidentiality, thus leaving the petitioner-client without the ability to introduce evidence of his attorney’s alleged misconduct. The Court expressly invited the legislature to reconsider the strictness of Evidence Code Section 1119. Justice Chin’s concurrence acknowledged that shielding attorneys from being held accountable for negligent or fraudulent conduct during mediation “is a high price to pay to preserve total confidentiality in the mediation process.”¹¹

In contrast to *Facebook* and *Cassel*, which upheld mediation confidentiality as absolute, a recent Second Circuit opinion, *In re Teligent*,¹² found that limited exceptions do exist. In *Teligent*, the parties had agreed to be bound by protective orders that imposed limitations on disclosure of communications made in mediation. The Second Circuit held that lifting the protective orders to allow for disclosure of mediation communications would be warranted only if the party seeking disclosure could establish three conditions: (1) a special need for the confidential material, (2) resulting unfairness from lack of discovery, and (3) the need for the evidence outweighed the interest in maintaining confidentiality.¹³

Is the Second Circuit's recent opinion sanctioning exceptions to strict mediation confidentiality likely to influence California's viewpoint on mediation confidentiality? *Facebook* from the Ninth Circuit, *Cassel* from the California Supreme Court, and *Kieturakis* all indicate that the answer is no. These cases preserve strict adherence to the doctrine of mediation confidentiality. Their holdings represent, at this time, both the legislative and judicial embodiment of California's public policy.

II. THE ENSHRINED PUBLIC POLICY OF SPOUSAL FIDUCIARY DUTY

Evolution of the spousal fiduciary duty embodied in Family Code Section 721 has been a major development in the field of family law during the past decade.¹⁴ As illustrated below, California courts have consistently upheld the sanctity of spousal fiduciary duty as a matter of public policy.

In *In re Marriage of Burkle*,¹⁵ the Court of Appeal held that the parties' 1997 postnuptial agreement was valid and enforceable because mutual reciprocal advantages existed. *Burkle* teaches three important lessons. First, a presumption of undue influence does not arise in an interspousal transaction unless one spouse obtains an "unfair" advantage – a mere advantage is not enough. By drawing this distinction, the court narrowed the scope of the fiduciary duty between spouses. Second, even if a presumption of undue influence arises, it may be rebutted. Third, the statutory requirement that parties to a dissolution proceeding serve Declarations of Disclosure does not apply to spouses who execute a postnuptial agreement when no imminent dissolution of the marriage is anticipated.

In *In re Marriage of Feldman*,¹⁶ the husband was sanctioned for his failure to update disclosures and provide the wife with information regarding his financial dealings during their marital dissolution proceeding. *Feldman* teaches that if you do not

keep disclosures properly updated to reflect material changes in assets or debts, you will be sanctioned pursuant to Family Code Section 2107.

*In re Marriage of Fossum*¹⁷ held that a wife who took a cash advance on a credit card without disclosing the fact to her husband violated her fiduciary obligation to him under Family Code Section 721. The Court of Appeal also held that where a breach of spousal fiduciary duty has been established, an award of attorney's fees is mandatory under the provisions of Family Code Section 1101(g).

*In re Marriage of Margulis*¹⁸ is an important recent opinion concerning the burden of proof for establishing a breach of spousal fiduciary duty. That case held that when the non-managing spouse presents *prima facie* evidence that community assets have disappeared while under the control of the managing spouse post-separation, the burden of proof shifts to the managing spouse to account for the missing assets, or that spouse will be charged for their value. Family Code provisions impose on the managing spouse "...affirmative, wide-ranging duties to disclose and account for the *existence, valuation, and disposition* of all community assets from the date of separation through final property division."¹⁹ The fiduciary relationship between spouses requires the managing spouse to reveal any self-dealing or other conduct that impaired the value of the property and entitles the other spouse to compensation. *Margulis* reinforces the duty of spouses to account for assets under their management and control, strengthening the doctrine of the fiduciary duty owed by one spouse to the other.

III. CLASH OF PUBLIC POLICIES – HOW TO RESOLVE THE CONFLICT

A. Argument that Spousal Fiduciary Duty Prevails

Litigants contending that spousal fiduciary duty should prevail over mediation confidentiality must distinguish the facts of *In re Marriage of Kieturakis*, which is the only authority to hold that the presumption of undue influence does not apply to mediated settlement agreements.²⁰ In *Kieturakis*, the wife challenged the parties' mediated settlement agreement, alleging fraud, duress and lack of disclosure, but, at the same time, refused to waive mediation confidentiality. The trial court found that the husband had the burden of proof, based on the presumption of undue influence that attaches to unequal marital transactions. The wife's refusal to waive mediation confidentiality would have prevented the husband

from meeting his burden. Commenting that it was confronted with the most difficult legal issue it had ever faced, the trial court admitted evidence from the mediation on the ground it had to do so in the spirit of fairness and justice, and ruled in favor of the husband.

The Court of Appeal affirmed, but found that husband did not have to rebut the presumption of undue influence because the presumption does not apply to mediated settlement agreements. According to the appellate court, policies favoring mediation and finality of judgments trump the presumption of undue influence and the concept of spousal fiduciary duty. The court further held that the burden of proving undue influence under such circumstances is placed upon the party seeking to set aside a mediated agreement under Family Code Section 2122.

It is important to note that *Kieturakis* did not hold that mediation evidence can never be admissible. *Kieturakis* acknowledged that *Olam v. Congress Mortgage Co.*²¹ created a nonstatutory exception to mediation confidentiality when a balancing of the need to do justice in a particular case against policies favoring mediation weighs in favor of compelling a mediator to testify. Although *Kieturakis* states that *Olam* is “questionable authority,” given the California Supreme Court’s refusal in *Foxgate* and *Rojas* to recognize nonstatutory or good cause exceptions, it expressly leaves open the question of *Olam*’s continued viability. “We need take no position on *Olam*’s viability because the outcome would be the same in this case whether or not the decision to compel evidence from the mediator could be sustained. . . Here, as in *Olam*, the mediator could be seen as the source of the most probative evidence on the merits of the parties’ dispute, and compelling that evidence could be viewed as doing relatively little damage to mediation confidentiality.”²² Thus, it can legitimately be contended that the court left open the possibility that mediation evidence could be admissible in some circumstances, even absent a waiver of the mediation privilege.

Given the protected status of spousal fiduciary duty and the public policy it was designed to protect (Family Code §§ 721 and 1100), it remains a colorable argument that limitations on spousal fiduciary duties and remedies should be created by the Legislature, not the courts. As the California Supreme Court noted in *Rojas v. Superior Court*, “. . . the Legislature clearly knows how to establish a ‘good cause’ exception to a protection or privilege if it so desires.”²³

Kieturakis was questioned in a thoughtful law review article,²⁴ which observed that “critics of *Kieturakis* object to fixed rules favoring mediation confidentiality over other important policies. . . [and] have expressed concern about the potential consequences that will result if mediated agreements are ‘effectively exempt from the established standards [of contract common law].’ The chief concern of this view relates to the potential for parties to abuse the system, in that ‘an individual intending abusive negotiation strategies like fraud or coercion could insist on negotiating in a mediation and then cling to his right of confidentiality when enforcing the suspect agreement.’ ”²⁵ The article contrasts the inflexible, bright-line approach taken in *Kieturakis* with a balancing-test approach, which stresses “the need for judicial discretion based on the circumstances of each case, while insuring a basic level of confidentiality by calling for in camera review of the confidential material.” Under this approach, “even if a judge determined that the ‘need for mediation evidence’ outweighed the purposes served by confidentiality, the mediation evidence in question would not become a matter of public record, but would be disclosed to the judge(s) only,” thereby “afford[ing] more protection than would a rule of bare disclosure.”²⁶ While questioning “whether the flexibility gained by a balancing approach would outweigh the loss of the full protection of confidentiality and the lack of a uniform legal rule,” the author surmised that if a balancing approach were adopted, “California judges could use their discretion to shape a discernible rule by identifying some specific factors relevant to each side of the balance.”²⁷ Attorneys contending that spousal fiduciary duty should prevail over a strict application of mediation confidentiality can (under *Olam* and *Rinaker*) and should argue that the court should adopt a balancing approach.

Courts have long been faced with deciding between competing public policies and presumptions. The California Supreme Court did so in *In re Marriage of Schnabel*²⁸ where it employed a balancing test to weigh a spouse’s need for discovery against the financial privacy interests of a third party. In a similar vein, courts must at times decide between competing presumptions and burdens of proof. For example, in *In re Marriage of Haines*,²⁹ the court held that when the title presumption in Evidence Code Section 662 conflicts with the presumption of undue influence in Family Code Section 721, the presumption of undue influence must prevail.

Likewise, in *Marriage of Margulis*, discussed above, the court was faced with competing burdens of proof under Evidence Code Section 500³⁰ and Family Code Section 721. *Margulis* “illustrates the importance of shifting to the managing spouse the burden of proof on missing assets ... [as well as] how shifting this burden of proof furthers the statutory purposes of requiring complete transparency and accountability in the management of community assets and of providing a remedy to the nonmanaging spouse when a breach of that fiduciary duty occurs.”³¹ *Margulis* arguably suggests that the presumption of undue influence should have been applied in *Kieturakis*, and that the burden of proof should be on the spouse who allegedly gained an advantage through a transaction with his wife. Perhaps the *Margulis* opinion evidences a shift in California towards a heightened judicial propensity to elevate the importance of the doctrine of spousal fiduciary duty.

B. Argument that Mediation Confidentiality Should Prevail

Those litigants contending that the doctrine of mediation confidentiality should prevail will argue that mediation confidentiality must protect all communications that take place during mediation, regardless of whether such communications allegedly constitute fraud, misrepresentation or breach of fiduciary duty. In the context of a mediation between spouses, evidence of a breach of fiduciary duty would remain precluded by mediation confidentiality, leaving the spouse against whom the breach was committed without the ability to prove his or her case, and thus, without a remedy.

Two core arguments support this position. First, the policy of mediation confidentiality is embodied in Evidence Code 1119, as referenced above. In *Foxgate*,³² the California Supreme Court held: “...there are no exceptions to the confidentiality of mediation communications or to the statutory limits on the content of mediator’s [sic] reports. Neither a mediator nor a party may reveal communications made during mediation.” Thus, absent an express statutory exception or an express written waiver, disclosure of communications made during mediation is prohibited. The result of this, of course, is that one party has control over the other party’s ability to present evidence. In some cases, this means that one spouse, who owes the highest duty of good faith and fair dealing to the other spouse, can exercise substantial control over the outcome of disputes concerning mediated marital agreements.

Second, *In re Marriage of Kieturakis*³³ stands for the proposition that the presumption of undue influence in marital transactions must yield to the policy favoring mediation confidentiality. Under *Kieturakis*, the party challenging the mediated marital agreement shoulders the burden of proof, as noted above. That burden may be impossible to meet if the party is precluded from introducing evidence of any communication, writing, or negotiation that took place during mediation. Proponents of mediation confidentiality will therefore argue for a broad interpretation of *Kieturakis*.

Against the backdrop of these *Kieturakis*-supported arguments, a nonsuit pursuant to Code of Civil Procedure Section 581c is a potential, aggressive procedural option.³⁴ A motion for nonsuit can be made after an opening statement and serves as a demurrer to the introduction of evidence.³⁵ Proponents of this proactive procedure will contend that a nonsuit is appropriate because the subject agreement was negotiated and consummated during the course of mediation. Assuming the parties have not both expressly waived mediation confidentiality under Evidence Code Section 1122(a)(1), anything said during mediation is inadmissible. The only document admissible is the agreement itself, pursuant to Evidence Code Section 1123(b). This results in a core problem for the challenging party because either (a) the challenging party must rely on inadmissible evidence precluded by mediation confidentiality to establish his or her *prima facie* case; or (b) the party opposing the contract challenge is precluded by mediation confidentiality from putting on exculpatory defense evidence. That preclusion itself acts to prevent the challenging party from putting on a *prima facie* case, thus the possibility of a non-suit as a matter of law.

IV. CONCLUSION

In re Marriage of Kieturakis appears to make it almost impossible to invalidate a mediated agreement between spouses, in spite of a breach of fiduciary duty. Clients seeking to uphold such an agreement will rely on *Kieturakis* and maintain that tearing the fabric of the firm judicial curtain protecting mediation confidentiality would be detrimental to couples who wish to resolve their differences through the favored process of mediation. Breaking this rigid judicial barrier of mediation confidentiality might arguably discourage alternative dispute resolution and potentially lead to increased litigation in a state where courts already face financial shortfalls and overly burdened courtrooms.

On the other hand, the rigid bright-line rule imposed by *Kieturakis* could very well deter couples from even considering mediation, for fear that if fraudulent misrepresentation occurs, the mediated agreement will nevertheless be upheld. To address this not unreasonable concern, courts should not automatically reject the presumption of undue influence, as this would severely limit, if not completely eliminate, the fiduciary duties one spouse owes to the other as a matter of law. The burden of proving a breach of fiduciary duty should not shift solely on reliance on the narrow reasoning of the *Kieturakis* opinion. The more recent case of *In re Marriage of Margulis*,³⁶ which places the burden of proof squarely on the party alleged to have committed the breach (though not citing *Kieturakis*), provides legal authority to support this view. A more nuanced approach would have the courts employ a balancing test on a case-by-case basis to weigh the two competing public policies in order to achieve ultimate fairness, which is, after all, the correct public policy goal.

This tension between strict application of one public policy doctrine and a balancing test that takes into account another equally sanctified public policy doctrine is not unknown to tradition, literature,³⁷ or the law. The phrase “quality of mercy” appears in many cases expounding equitable principles.³⁸

California practitioners have not seen the last word on the resolution of the tension between mediation confidentiality and breach of spousal fiduciary duty. Resolution may not come readily from the Legislature (as invited by the Supreme Court in *Cassel*), it may not come unbidden from the courts, but the progenitor of its ultimate resolution will surely come from the work of concerned, competent, creative California lawyers.

¹ $E=mc^2$, where E is energy, m is mass and c is the speed of light in a vacuum. Albert Einstein proposed his mass-energy equivalence equation in 1905. In physics, mass-energy equivalence is the concept that the mass of a body is a measure of its energy content. Even the imitable laws of physics are susceptible to technological re-interpretation. Neutrinos, subatomic particles moving faster than the speed of light, were reported last year. If substantiated, this discovery would upend the foundation of modern physics. [Lemonick, Michael D. “Faster than Light: A new study may upend Einstein.” *Time* 10 Oct. 2011:17]. Now you know why we are lawyers, not physicists.

² *In re Marriage of Kieturakis* (2006) 138 Cal.App.4th 56.

³ *Rinaker v. Superior Court* (1998) 62 Cal.App.4th 155.

⁴ *Olam v. Congress Mortgage Co.*(1999) 68 F.Supp.2d 1110.

⁵ See *In re Marriage of Kieturakis*, supra, 138 Cal.App.4th at 77-78 (citing both *Rinaker v. Superior Court* and *Olam v. Congress Mortgage Co.*).

⁶ Section 721(b) provides that “in transactions between themselves, [spouses] are subject to the general rules governing fiduciary relationships which control the actions of persons occupying confidential relations with each other” and which impose “the highest duty of good faith and fair dealing” in such transactions.

⁷ *Facebook, Inc. v. Pacific Northwest Software, Inc* (2011) 640 F. 3d 1034.

⁸ *Id.* at 1042.

⁹ *Cassel v. Superior Court* (2011) 51 Cal.4th 113.

¹⁰ See *Foxgate Homeowners’ Assn., Inc. v. Bramalea California, Inc.* (2001) 26 Cal.4th 1; *Rojas v. Super. Ct. (Coffin)* (2004) 33 Cal.4th 407; *Fair v. Bakhtiari* (2006) 40 Cal.4th 189; *Simmons v. Ghaderi* (2008) 44 Cal.4th 570.

¹¹ *Cassel*, supra, 51 Cal.4th at 138.

¹² *In re Teligent*, 640 F.3d 53(2d Cir. 2011).

¹³ *Id.* at 58.

¹⁴ Earlier fiduciary duty cases are discussed at length in the authors’ previous article regarding spousal fiduciary duties. See Marshall S. Zolla and Deborah Elizabeth Zolla, *Marital Duty*, Los Angeles Lawyer (February 2004).

¹⁵ *In re Marriage of Burkle* (2006) 139 Cal.App.4th 712.

¹⁶ *In re Marriage of Feldman* (2007) 153 Cal.App.4th 1470.

¹⁷ *In re Marriage of Fossum* (2011) 192 Cal.App.4th 336.

¹⁸ *In re Marriage of Margulis* (2011) 198 Cal.App.4th 1252.

¹⁹ *Id.* at 340.

²⁰ *In re Marriage of Kieturakis*, supra, 138 Cal.App.4th 56.

²¹ *Olam*, supra, 68 F.Supp.2d 1110.

²² *Kieturakis*, supra, 138 Cal.App.3d at 94.

²³ *Rojas v. Superior Court*, supra, 33 Cal.4th at 423.

²⁴ Annalisa L. H. Peterson, *When Mediation Confidentiality and Substantive Law Clash: An Inquiry into the Impact of In re Marriage of Kieturakis on California’s Confidentiality Law* (2007) 8 Pepp. Disp. Resol. L.J. 199.

²⁵ *Id.* at 206, quoting Peter Robinson, *Centuries of Contract Common Law Can’t Be All Wrong: Why the UMA’s Exception to Mediation Confidentiality in Enforcement Proceedings Should be Embraced and Broadened* (2003) 2003 J. Disp. Resol. 135, 138 (2003).

²⁶ *Id.* at 208, quoting Ellen Deason, *Enforcing Mediated Settlement Agreements: Contract Law Collides with Confidentiality* (2001) 35 U.C. Davis L. Rev. 33, 102.

²⁷ *Id.*

²⁸ *In re Marriage of Schnabel* (1993) 5 Cal.4th 704.

²⁹ *In re Marriage of Haines* (1995) 33 Cal.App.4th 277.

³⁰ *Evidence Code* Section 500 provides: “Except as otherwise provided by law, a party has the burden of proof as to each fact the existence or non-existence of which is essential to the claim for relief or defense that he is asserting.”

³¹ *In re Marriage of Margulis*, supra, 198 Cal.App.4th at 1274.

³² *Foxgate Homeowners’ Ass’n, Inc. v. Bramalea California, Inc.*, supra, 26 Cal.4th at 4.

³³ *In re Marriage of Kieturakis*, supra, 138 Cal.App.4th at 56.

³⁴ This occurred in the trial court in *In re Marriage of Musk* (Los Angeles Superior Court Case No. BD487602) in May 2010.

³⁵ *Code of Civil Procedure* § 581c(a); *Darr v. Lone Star Industries, Inc.* (1979) 94 Cal.App.3d 895, 899.

³⁶ *In re Marriage of Margulis*, supra, 198 Cal.App.4th at 1252.

³⁷ See Portia’s “quality of mercy” speech in *The Merchant of Venice*, Act IV, Scene 1, 185.

³⁸ See, for example, *Fields v. Brown* (9th Cir. 2007) 503 F.3d 755; citing and quoting from *Mayfield v. Woodford* (2001) 270 F.3d 915.