

# Marital Property Law in Wisconsin

Fourth Edition

Volume I

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## Notes on the Fourth Edition

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The fourth edition of *Marital Property Law in Wisconsin* incorporates the statutory and common law developments affecting marital property in Wisconsin that were reported on in the 2005 and 2007 supplements and adds new material reflecting cases that have been issued and statutes that have been amended since the 2007 supplement. Among the most significant developments are U.S. Supreme Court cases concerning bankruptcy-law restrictions on attorneys and spouses' rights under employee-benefit plans and Wisconsin Supreme Court and Court of Appeals cases on marital property agreements, divisibility of assets, and exclusivity of the Wisconsin Marital Property Act's remedies. The book contains updated sample forms. All case citations, statutes, and regulations have been updated, as have the index and the appendices.





# Preface

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*Marital Property Law in Wisconsin* has been a leading source of information regarding Wisconsin's community property system for more than 25 years. Attorneys and courts alike have relied on this book for guidance on marital property matters, and we are confident that the fourth edition of this book will prove to be an influential, as well as a practical, resource for those wading into the thicket of marital property law.

On behalf of the State Bar of Wisconsin, we express sincere thanks to the authors for their efforts in updating and improving this book.

We also wish to recognize members of the State Bar CLE Books staff for their role in the development of this new edition. Thanks are due to Attorney-Editor Margie DeWind for her editorial work and for shepherding the book to publication; and to Jackie Johnson and Lana Ferstl for coordinating the production of the revision.

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# Foreword

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More than 26 years ago—on April 4, 1984—Wisconsin became the ninth community property state in the United States by enacting the Wisconsin Marital Property Act. The first edition of this book was published at the end of 1984 in response to that historic legislation. A second edition followed in November of 1986 after enactment of a “Trailer Bill” on October 22, 1985. The book was periodically supplemented thereafter and was completely revised and rewritten in 2004. This is the revised fourth edition.

The six original authors of this book (Judge McGarity, and Messrs. Christiansen, Haberman, Haydon, Kinnamon, and Wilcox) were members of the State of Bar of Wisconsin Special Committee on Marital Property, which existed between April 1979 and the passage of the Wisconsin Marital Property Act. Additional authors (Messrs. Halley, Herbach, Smith, and White) have come on board as the result of retirements or the need to secure greater in-depth coverage of substantive areas treated by the book.

In the preface to the first edition, we noted that the subject matter was new and complex, pervading the day-to-day practice of law. Although the subject matter is no longer new, it remains complex and pervasive. It is the authors’ hope that this book will continue to assist attorneys understand Wisconsin’s community property law.

The book provides considerable in-depth analysis of issues with community property law implications, but it is not exhaustive. We have tried to indicate where questions exist and have used our best judgment in providing answers. Although some case law interpretations and some additional statutory changes have occurred in the intervening 25 years since the enactment of the Wisconsin Marital Property Act, there remain many areas where there is little or no precedent upon which to rely.

This book is intended to be a working tool for attorneys seeking information about Wisconsin’s community property law. As we indicated 25 years ago, we hope that it will stimulate thinking about the subject,

and we are very appreciative of readers contacting us with new ideas and comments about the book.

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June 2010

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# 1

## Introduction; History; Basic Principles; and Constitutionality

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## I. History [§ 1.1]

### A. Introduction [§ 1.2]

On April 4, 1984, the Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or the Wisconsin Marital Property Act], became law. Eight months earlier, in July 1983, the National Conference of Commissioners on Uniform State Laws approved the Uniform Marital Property Act (1983) at its annual conference. Although the Wisconsin Act is derived from UMPA, it differs from UMPA in many important respects. The Wisconsin Act also has its own unique history that differs from the history underlying UMPA.<sup>1</sup>

➤ **Note.** The Uniform Marital Property Act [hereinafter UMPA], is reprinted in appendix A, *infra*. To date, no other state has enacted UMPA or any version of it. Also, UMPA has not been amended since its promulgation in 1983.

When the Wisconsin Marital Property Act was enacted on April 4, 1984, it was understood and explicitly stated that a trailer bill would be necessary to implement the legislation. Two months later, in June 1984, the Legislative Council, whose members consist of legislators from both houses, created the Special Committee on Marital Property Implementation. The special committee, with the help of the Legislative Council, immediately began working on a trailer bill.

On April 10, 1985, the first trailer bill to the Act was introduced as 1985 Senate Bill 150. When, after several months, the legislature remained deadlocked over the bill, a Committee of Conference was appointed. On October 8, 1985, the committee issued its report, which recommended that the legislature adopt and concur in Conference Substitute Amendment 1, which was attached to the report. Both houses accepted the conference report, and the trailer bill as amended by the

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<sup>1</sup> Unless otherwise indicated, all references to the Wisconsin Statutes are current through the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189. Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

Committee of Conference was enacted on October 22, 1985, as 1985 Wisconsin Act 37 [hereinafter 1985 Trailer Bill]. (Links to bills affecting the Act are provided in appendix B, *infra*). The 1985 Trailer Bill did not change the Act's original effective date (January 1, 1986). The special committee was reauthorized by the Legislative Council during the 1985 and 1987 legislative sessions and was responsible for recommending a second trailer bill to the Act. 1987 Wisconsin Act 393 [hereinafter 1988 Trailer Bill].

In May 1988, the Legislative Council reestablished the special committee, for the purpose of preparing a third trailer bill. *State of Wisconsin Blue Book 1989–90*, at 395. The special committee was divided into two working groups: one studying the relationship of the marital property law to divorce, and one studying marital property implementation in general. Additional trailer legislation was introduced but not enacted. The special committee was continued for the 1991 legislative session, however, and a third trailer bill, 1991 Wisconsin Act 301 [hereinafter 1992 Trailer Bill], was passed in 1992. The 1992 Trailer Bill became effective May 14, 1992.

In addition to enacting the 1992 Trailer Bill, the legislature enacted 1991 Wisconsin Act 224, which amended provisions of the Probate Code to make changes in the nature of deferred marital property for intestate estates. The special committee was not continued following the 1991 legislative session. Nonetheless, the legislature has continued to make changes to the provisions of the law.

1993 Wisconsin Act 160 changed the treatment of individual retirement account (IRA) assets traceable to a rollover from a deferred-employment-benefit plan in the case of marital property assets.

The comprehensive revisions to the Probate Code under 1997 Wisconsin Act 188, effective January 1, 1999, included a wholesale revision to the former deferred marital property election against probate assets and the augmented marital property estate election against nonprobate assets. For a discussion of the elections before 1999, see section 12.135, *infra*. The former elections have been combined into a single deferred marital property election under section 861.02, which applies to both probate and nonprobate assets and which provides for a pecuniary amount rather than an item-by-item election.

2005 Wisconsin Act 216 amended several provisions of chapter 766 and corresponding provisions of the Wisconsin Probate Code, discussed at various places in chapters 2, 10, and 12, *infra*.

## **B. Overview of the History of Community Property at the National Level [§ 1.3]**

The debate over whether a state should have a common law property system or a community property system was not new when the Wisconsin Legislature began to study the issue. For example, during the California constitutional convention in 1849, one of the issues debated was whether California should adopt a separate property system or a community property system. The debate is described in Scott Greene, *Comparison of the Property Aspects of the Community Property and Common Law Marital Property Systems and Their Relative Compatibility with the Current View of the Marriage Relationship and the Rights of Women*, 13 Creighton L. Rev. 71, 76 (1979). Another account of the debate is reproduced in William A. Reppy, Jr., *Community Property in California* 9 (1980).

In 1936, Professor Richard Powell published an article, *Community Property—A Critique of Its Regulation of Intra-Family Relations*, 11 Wash. L. Rev. 12 (1936), in which he compared the common law system to the community property system. He found

the community property system lacking as a system of marital property. Its complexity is such as not to be offset by those values claimed for it by its most ardent protagonists. It injects useless uncertainty and unjustifiable barriers into transactions between the spouses as a unit and third persons. It submerges the individual husband or wife in a purely imaginary third entity—the family, in a fashion promoting the ultimate welfare of no one except those parasites who live on litigation-breeding rules of law and have no care for the social implications of the statutes and decisions of their jurisdiction. The writer realizes that many may be shocked at his disregard of the alleged protection of helpless wives implicit in this system. Somehow he cannot bring himself to believe that the husbands of California and of Washington are more ruthless, less loving, than the husbands of Pennsylvania and New York. The wives of those two old states have not found themselves suffering under the closest approach to the individualistic standard yet existent in any of these United States. The vaunted protection of married women is an intellectual hangover from the time when woman



was a salable chattel and ill consorts with the modernity and wisdom otherwise so characteristic of the West Coast.

*Id.* at 38 (footnote omitted).

In 1967, Michael Vaughn also published a comparison, *The Policy of Community Property and Inter-Spousal Transactions*, 19 Baylor L. Rev. 20 (1967). He said:

In summary, the policy of community property is basically one of equality. The husband and wife are to be accorded the status of equals, because of the actual contribution that each makes to the marriage—because of their status as partners in a “marital partnership based on the view that two individuals are equally devoting their lives and energies to furthering the material as well as the spiritual success of marriage.” The partnership purpose is to create a successful marriage, and a concise statement of the policy of community property is that it is to treat the spouses as equals because of the actual contribution of each to the accomplishment of the partnership purpose.

*Id.* at 40–41.

A wave of reform relating to the property rights of married women occurred in the United States in the mid-1800s in the form of the Married Women’s Property Acts. In 1839, Mississippi became the first state to adopt such an act. Wisconsin enacted its Married Women’s Property Act in 1850. These acts generally permitted women to own their own property as separate property, make contracts, engage in business, sue or be sued, be liable for their own debts, and so forth.

The next significant waves of reform relating to the property rights of married women did not occur until more than 100 years later, in the 1970s. At that time, no-fault divorce and equitable division (also called equitable distribution) at divorce swept through most of the 50 states. See Doris Jonas Freed & Henry H. Foster, *Divorce in the Fifty States: An Overview As of 1978*, 13 Fam. L.Q. 105 (1979).

During the same period, a different wave of reform moved through the eight community property states: the concept of equal management and control. Before 1967, all eight community property states provided for male management of community property. A Louisiana statute, for example, expressly provided that the husband was the “head and master of the partnership.” In 1967, Texas became the first community property

state to amend its law to provide that each spouse could manage the property that he or she could manage if single. Between 1972 and 1980, the other seven community property states changed their laws to provide for equal management of community property by husband and wife. An excellent history of the community property reform movement is contained in Cantwell, *Man + Woman + Property = ?*, 6 Prob. Law. (1980).

➤ **Comment.** Effective January 1, 1980, the Louisiana statute was changed to grant spouses equal rights in the disposition of community property. On March 23, 1981, the U.S. Supreme Court declared the “head and master” statute unconstitutional on the ground it constituted gender-based discrimination. *Kirchberg v. Feenstra*, 450 U.S. 455 (1981).

In 1983, the National Conference of Commissioners on Uniform State Laws adopted UMPA. UMPA created a community property system that essentially treats spouses as partners at all times in the marriage: during marriage, at divorce, and at death.

Effective as of May 23, 1998, Alaska adopted the Alaska Community Property Act, codified in title 34, chapter 77, of the Alaska Statutes. Under the Alaska Community Property Act, property of spouses is classified as community property only to the extent provided in a community property agreement or a community property trust. Alaska Stat. § 34.77.030 (current through the 2009 First Regular Session and the First Special Session of the 26th Legislature). Whether property classified as community property under the Alaska elective system of community property will be regarded as community property for federal tax purposes (and in particular I.R.C. § 1014(b)(6)) is questionable.

### **C. The Role of Congressional Tax Policy [§ 1.4]**

In addition to the property law reforms briefly discussed in the preceding section, Congress’s enactment and amendment of the Internal Revenue Code has played an important role in the development of community property law in the United States.

The federal income tax was authorized by the 16th Amendment to the U.S. Constitution in February 1913. Thirteen years later, in *United States v. Robbins*, 269 U.S. 315 (1926), the U.S. Supreme Court was

faced with the question of whether spouses in California should report their income separately, one-half each. If spouses reported their community income on two separate returns, this income splitting would result in significant income tax benefits to couples in California. The Court held that the wife's interest in community income was a "mere expectancy" and ruled that the wage-earning spouse should report all the income, not just half of it.

Because of *Robbins*, California changed its community property law to clarify that each spouse had "present, existing and equal interests" in community property assets. This change led to the issue of income splitting again being considered by the U.S. Supreme Court. (One year earlier, in four test cases, the Supreme Court had decided that residents in four other community property states could file separate returns. *See Poe v. Seaborn*, 282 U.S. 101 (1930) (Washington); *Goodell v. Koch*, 282 U.S. 118 (1930) (Arizona); *Hopkins v. Bacon*, 282 U.S. 122 (1930) (Texas); *Bender v. Pfaff*, 282 U.S. 127 (1930) (Louisiana).) This time, in *United States v. Malcolm*, 282 U.S. 792 (1931), the Court ruled that each spouse owned half the earned income and that the earned income should be split for income tax purposes.

The tax advantages of income splitting enjoyed by residents of community property states caused some common law states to follow California's lead and consider switching to a vested community property system. In 1939, Oklahoma adopted a conventional (also called elective) community property system. However, the U.S. Supreme Court decided in *Commissioner v. Harmon*, 323 U.S. 44 (1944), that conventional (or elective) community property is an assignment of income for income tax purposes that makes income splitting impermissible. After *Harmon*, there was a flurry of legislative activity between 1945 and 1947, when Oklahoma, Hawaii, Oregon, Nebraska, Michigan, and Pennsylvania all adopted mandatory (also called legal) community property systems to achieve income splitting for their residents. Similar bills were pending in other state legislatures, including Wisconsin's.

The adoption of legal community property systems by some of the common law states prompted the Revenue Act of 1948, Pub. L. No. 80-471, 62 Stat. 111. The purpose of the 1948 act was to provide parity between the community property states and the common law states. The act provided for:

1. The option of joint income tax filing by spouses as an alternative to separate filing;
2. A marital deduction for federal estate tax purposes (under this deduction, half the predeceasing spouse's estate could be left to the surviving spouse tax free);
3. A full adjustment in basis for both halves of community property when one spouse dies;
4. A marital deduction for gift tax purposes; and

➤ **Historical Note.** As originally adopted and until 1976, the gift tax marital deduction was substantially different from the estate tax marital deduction. Under the estate tax marital deduction, one spouse could give half of his or her total assets to the other spouse tax free. However, under the gift tax marital deduction, one spouse could only give half of *each item* to the other spouse tax free. Therefore, under the estate tax marital deduction, one spouse could retain half the estate and transfer the other half to the surviving spouse tax free. By contrast, under the gift tax marital deduction, if one-half of the estate was left to the other spouse, only half of the half, or one-fourth of the whole, would be tax free.

5. Gift splitting under which a gift by one spouse to a third party was treated as having been made by both spouses if the nondonee spouse joined in the gift.

See chapter 9, *infra*, for a discussion of tax issues.

The 1948 Revenue Act ended the common law states' experiments with community property. However, the cycle would start again 14 years later, after the U.S. Supreme Court decided *United States v. Davis*, 370 U.S. 65 (1962). In *Davis*, the Court ruled that an unequal division of legally owned assets between spouses as a result of a divorce was a sale or exchange for capital-gains tax purposes. Again, as when they reacted to the *Poe* and *Malcolm* decisions, the common law states desired the tax benefits of the community property system. In a community property system, co-ownership of assets by spouses is more prevalent, so there are fewer *Davis*-type problems, and capital-gains tax consequences are less severe. Colorado, Oklahoma, Kansas, and some other states reacted to

the *Davis* rule by creating a species of common property ownership arising at the commencement of the divorce proceeding. *See, e.g.*, Minn. Stat. § 518.003 (subd. 3b) (West, WESTLAW current with laws of the 2010 Regular Session through Chapter 188); Mo. Stat. § 452.330 (West, WESTLAW current through the end of the 2009 First Regular Session of the 95th General Assembly); N.C. Gen. Stat. § 50-20(k) (West, WESTLAW current through S.L. 2009-577 (end) of the 2009 Regular Session); *Imel v. United States*, 523 F.2d 853 (10th Cir. 1975) (Colorado); *Collins v. Commissioner*, 412 F.2d 211 (10th Cir. 1969), and *Collins v. Oklahoma Tax Comm'n*, 446 P.2d 290 (Okla. 1968) (Oklahoma); *Cady v. Cady*, 581 P.2d 358 (1958) (Kansas). This species of property was akin to community property.

Congress overruled *Davis* when it enacted the Tax Reform Act of 1984, Pub. L. No. 98-369, 98 Stat. 494. The fact that both the Revenue Act of 1948 and the Tax Reform Act of 1984 extended tax benefits enjoyed by community property states to the common law states following experimentation by the common law states is striking.

The Internal Revenue Code played one additional role in facilitating change from a common law property system to a community property system. Community property reform began to gain momentum in the middle and late 1970s. However, the federal gift-tax law was a serious impediment to enactment of a community property system by a common law state because a change to a community property system at that time would have resulted in transfers of ownership between spouses, which most likely would have been subject to federal gift tax. Richard W. Bartke, *Marital Sharing—Why Not Do It By Contract?*, 67 Geo. L.J. 1131 (1979). However, in 1976, Congress liberalized the federal gift-tax law by passing the Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520. In 1981, Congress completely eliminated gift tax on qualifying interspousal gifts by passing the Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, 95 Stat. 172. Thus, serious tax impediments to the adoption of a community property system were removed.

#### **D. Brief History of the Property Rights of Married Persons in Wisconsin [§ 1.5]**

The history of the property rights of married persons in Wisconsin has largely paralleled national developments, although Wisconsin has led the nation in some important respects.

➤ **Note.** For additional history on the adoption of a community property system in Wisconsin, see June Miller Weisberger, *The Wisconsin Marital Property Act: Highlights of the Wisconsin Experience in Developing a Model for Comprehensive Common Law Property Reform*, 1 Wis. Women's L.J. 5 (1985) (the first of two articles on the subject).

Wisconsin adopted its version of the Married Women's Property Act in 1850. 1850 Wis. Laws ch. 44. This Act was contained in chapter 766 of the 1981–82 Wisconsin Statutes. In 1921, the legislature enacted chapter 529 of the Laws of 1921, which added the following section to the Wisconsin Statutes:

**6.015 Women to Have Equal Rights.** (1) Women shall have the same rights and privileges under the law as men in the exercise of suffrage, freedom of contract, choice of residence for voting purposes, jury service, holding office, holding and conveying property, care and custody of children, and in all other respects. The various courts, executive and administrative officers shall construe the statutes where the masculine gender is used to include the feminine gender unless such construction will deny to females the special protection and privileges which they now enjoy for the general welfare. The courts, executive and administrative officers shall make all necessary rules and provisions to carry out the intent and proposes of this statute.

It has been stated that this statute was the first such equal-rights statute ever passed by a state legislature. Wisconsin Commission on the Status of Women, *Wisconsin Women and the Law* xi (3d ed. 1979). Section 6.015 subsequently became section 766.15.

In contrast to the federal income tax system, Wisconsin retained its system of separate income reporting for income tax purposes. After 1948, when the federal system was changed to permit joint filing, Wisconsin's separate-income-reporting system served as a reminder that Wisconsin had a common law property system.

In the 1970s, significant events contributing to the enactment of the marital property law occurred in all three branches of Wisconsin's government: executive, judicial, and legislative. These events are described in the following subsections.

## 1. Executive Branch [§ 1.6]

In January 1975, then Governor Patrick J. Lucey recreated the Governor's Commission on the Status of Women. The commission was originally created in 1964 in response to an "invitation to action" issued to the states in the 1963 report of the President's Commission on the Status of Women. The recreated Wisconsin commission began an examination of Wisconsin's laws as they applied to women. The commission published a number of influential reports and pamphlets that heightened interest in the subject. *See, e.g., The Marriage Partnership* (c. 1979); *Real Women, Real Lives: Marriage, Divorce, Widowhood* (1978); *That Old American Dream & the Reality Or Why We Need Marital Property Reform* (1977); *Toward A True Marriage Partnership* (1976); *Wisconsin Women: Know Your Rights* (1968); *Wisconsin Women and the Law* (3d ed. 1979). Other organizations also published materials about Wisconsin law and its application to women. *See, e.g., Irish, A Common Law State Considers a Shift to Community Property*, 5 Community Prop. J. 277 (1978) (supported by grants from the Smongeski Foundation and the Wisconsin Governor's Commission on the Status of Women); League of Women Voters of Wisconsin, *His ... Hers ... Theirs: Marital Property* (1978); Marygold Shire Melli, *The Legal Status of Homemakers in Wisconsin* (1977, Center for Women Policy Studies).

## 2. Judicial Branch [§ 1.7]

As the executive branch was examining Wisconsin's laws as they applied to women, several Wisconsin court decisions highlighted the key difference between a separate property system and a community property system. A good example is *Rasmussen v. Oshkosh Savings & Loan Ass'n*, 35 Wis. 2d 605, 151 N.W.2d 730 (1967). In that case, the husband earned wages and the wife worked in the home. The husband regularly turned his earnings over to his wife, who managed the family funds. Over the years, she deposited savings into separate savings accounts for each of their two sons. Each son was designated as beneficiary of the account for him. When the wife predeceased her husband, one son's account contained approximately \$1,800, and the other son's account contained approximately \$3,100. Upon learning of the existence of the two accounts after his wife's death, the husband brought suit claiming ownership of both accounts.

In a 4–3 decision, the Wisconsin Supreme Court held that the money in both accounts belonged solely to the husband:

Gifts from a husband to his wife are not presumed from the marital relationship but are governed by the same rules as gifts between strangers, namely, there must be an intention to part with the interest in and dominion over the property and there must be delivery of the property....

....

It is apparently a common practice in some American households for the husband, for the sake of convenience or for other reasons satisfactory to him, to turn over most or all of his earnings to his wife to meet the household and other expenses. The image of a housewife scrimping and saving some of this money is a popular one, but how much scrimping can be done by the wife depends in part upon the amount of funds turned over to her. A husband and wife may have an understanding that she is to receive an “allowance” for certain purposes and intend that any surplus shall belong to the wife. This is a kind of reward or incentive bonus for good management. Then too, the wife may, without any such definite understanding, be given funds for household purposes and the amount may or may not be sufficient; if not, she must ask for more. But if the allowance is sufficient or at times more than enough, one would think the surplus would still be impressed with the household purposes and be added to the amount of the next allowance.

In other situations, the wife may act as the “business manager,” handling all the finances for the family. Such control of the funds does not ordinarily give rise to a gift of any surplus after meeting family expenses, otherwise very few husbands would entrust their wives with the household finances. The general rule in separate-property states in which the husband and wife may own property separate from the other is that the excess left after paying the joint expenses of the husband, the wife, and the family, remains the property of the husband and does not automatically constitute a gift to the wife....

....

Where only the husband contributes the funds, the money earned by him is his property out of which he has a duty to support his family, and for this purpose he may make his wife the custodian of his earnings. But, in the absence of clear evidence to the contrary, the surplus after meeting such expenses remains his property.... Thus if a gift is to be found as the trial court did on the present facts, the evidence must be clear and convincing that the husband intended to make a gift of any excess to his wife.

....

The trial court believed the failure of the husband to inquire concerning the money he turned over to his wife was evidence of a gift. While such evidence is not inconsistent with a gift, there is no rule that a husband must keep a constant check upon his wife in her handling of funds lest any surplus be considered hers by default. The evidence here fails to sustain the burden of proof of showing intent to make a gift.



*Id.* at 609–12.

Another significant case is *Skaar v. Department of Revenue*, 61 Wis. 2d 93, 211 N.W.2d 642 (1974). When the case arose, Wisconsin's state income tax system required each spouse to report his or her income separately. The plaintiff spouses both worked on their farm and contributed to producing the farm income. They claimed they were partners, although they had never entered into a formal partnership arrangement, and each spouse reported one-half the income. The Wisconsin Department of Revenue assessed additional income taxes to Mr. Skaar on the grounds that he and his wife were not legal partners and that all the farm income was owned by the husband and taxable to him. In a 4–3 decision, the court said that

While the taxpayers may have desired to create a marital financial relationship similar to a partnership, it is clear they did not intend to create a bona fide partnership.

Initially, the parties to a partnership must intend to contractually form the legal relationship of a partnership. Such an intent is not shown here. While the W.T.A.C. [Wisconsin Tax Appeals Commission] found that the parties had reached an oral understanding, such oral understanding does not show the necessary intent. The oral understanding is more consistent with their marital relationship than with the existence of a bona fide partnership.

There do exist many indications that the taxpayers did not intend to create a bona fide partnership. They did not file partnership tax returns as required both federally and in Wisconsin. We think that if the taxpayers had intended to form a bona fide partnership they would not have violated the federal and Wisconsin legal requirement of filing. Likewise, the taxpayers failed to pay the federal self-employment tax for Mrs. Skaar which would have been required had such business arrangement been a partnership. Such tax surely would have been paid had the taxpayers intended to form a partnership and fulfill the legal requirements. The record discloses they were familiar with such requirements.

There are other indications the taxpayers did not intend to form a partnership. There was no automobile liability insurance coverage for Mrs. Skaar even though had a bona fide partnership been created, Mrs. Skaar would be liable for the tortious acts of her partner. Similarly, the books of the farm operation were not kept in a manner consistent with a bona fide partnership in that there was no division of the farming operation profits between the taxpayers. In fact, the lower court found that the taxpayers did not consider themselves partners in a legal sense.

The taxpayers argue that their desire to own everything together—their holding both farms in joint tenancy and their express desire to hold whatever personalty they own similarly—established the fact that they intended a partnership. Such is not the case. A partnership is not implied merely from

a common ownership of property. The fact that the community recognized Mrs. Skaar as possessing the authority to buy into the farming enterprise and that Mrs. Skaar helped manage and operate the farm are not in themselves controlling. Such facts are as common to a marital relationship as they are to a partnership. Further, whatever testimony that is adduced as to the agreement itself is necessarily self-serving.

... [T]he joint account into which all receipts, farm and other income are deposited is consistent with the relationship the taxpayers intend—that of marriage and not of partnership.

....

... We ... do not subscribe to the wisdom of income tax treatment of married persons in Wisconsin. We would prefer the federal system as it applies to married individuals. However, that is a matter for the legislature.

*Id.* at 99–101 (emphasis added and footnotes omitted).

Yet another important Wisconsin case is *Wisconsin Department of Revenue v. Kersten (In re Estate of Kersten)*, 71 Wis. 2d 757, 239 N.W.2d 86 (1976), concerning the inheritance tax. The spouses in that case owned most of their farm's assets as joint tenants. The husband predeceased the wife. At the time of his death, the Wisconsin inheritance tax law required the surviving joint tenant to pay inheritance tax on the full value of joint tenancy with one important exception. Under the exception, if any portion of the joint tenancy was acquired by the surviving spouse for adequate and full consideration in money or money's worth, the portion so acquired was exempt from inheritance tax. Therefore, the question was whether the wife acquired any portion of the joint farm assets for adequate and full consideration in money or money's worth.

The wife argued that she furnished consideration in the form of her services rendered on the farm. The Wisconsin Supreme Court agreed and held that the wife did furnish adequate and full consideration for the acquisition of the joint farm assets in an amount equal to half the value of the joint tenancy. Therefore, the court held that one-half the assets held in joint tenancy were exempt from the Wisconsin inheritance tax.

In 1985, approximately one year after the Marital Property Act was enacted, the Wisconsin Supreme Court decided *Krueger v. Department of Revenue*, 124 Wis. 2d 453, 369 N.W.2d 691 (1985). In that case, the husband had transferred his one-half interest in the family farm to his wife pursuant to a divorce agreement. The Wisconsin Department of Revenue asserted that he had transferred appreciated property to his wife

in exchange for a release of his marital obligations to her and assessed an additional \$10,879.98 in income taxes and interest. The husband challenged the assessment, claiming that the transfer to his wife was part of an overall equal division of their assets. In a 7–0 decision, the court said:

Because we conclude that Wisconsin statutes presume an equal ownership interest in property acquired during marriage, Krueger's transfer of appreciated property to his wife, pursuant to a divorce settlement in which each party received approximately one-half of the marital property, did not constitute a taxable event for Wisconsin income tax purposes.

....

... We conclude that Krueger's transfer of appreciated property was a nontaxable division of property: it operated to equally divide property he and his wife held under "a species of common ownership." ...

Krueger contends, and we agree, that the couple's property must be considered to be effectively co-owned, given the explicit legislative pronouncement of sec. 767.255, Stats., which presumes that upon the dissolution of a marriage all property which is not traceable to a gift or inheritance is to be divided equally between the parties except where specific factors are present to militate against such a division.... Thus, regardless of how the property which was acquired during the marriage may have been titled, each spouse in Wisconsin, since the statutory changes made effective in 1978, has presumptively an equal ownership interest in such property upon the dissolution of the marriage....

... We conclude that the best approach is to treat the transfer as a division by co-owners of jointly held property. Thus, the transfer does not result in a capital gain to the husband. Accordingly, the decision of the circuit court must be reversed.

*Id.* at 454–62.

In its opinion, the court referred to spouses as "equitable co-owners" of their property and said there was a trend toward viewing equitable-division statutes like section 767.255 (since renumbered as section 767.61) as creating a "constructive co-ownership of property," at least upon dissolution of the marriage. *Id.* at 461.

### **3. Legislative Branch [§ 1.8]**

During the 1970s, the Wisconsin Legislature took steps to reform the rights of women and the property rights of married persons. In 1971 and 1973, the Wisconsin Legislature adopted an equality-of-sexes

amendment to the Wisconsin Constitution, although it was defeated by popular vote in a referendum in April 1973. In the 1975–76 session, the legislature passed 1975 Wisconsin Laws Chapter 94, an omnibus law that eliminated gender-based distinctions in the Wisconsin Statutes. In the same session, the legislature passed a comprehensive sexual assault law (1975 Wis. Laws ch. 184) and a new inheritance tax statute (1975 Wis. Laws ch. 222). The latter codified the *Kersten* result and provided that joint-tenancy property was to be taxed as being owned one-half by each spouse, with the surviving spouse paying inheritance tax on half.

Also in 1975, a group of legislators, lawyers, and other interested persons formed a group to study women's issues and to advocate changing Wisconsin's property laws.

In the 1977–78 session, the legislature passed a no-fault divorce law and a law providing for equitable division of property at divorce. 1977 Wis. Laws ch. 105.

The first marital property reform bill, 1979 Assembly Bill 1090, was introduced in the Wisconsin Legislature in the 1979–80 session. Assembly Bill 1090 did not pass. In the 1981–82 legislative session, two bills were introduced: a community property bill (1981 Assembly Bill 370) and an alternative bill (1981 Assembly Bill 284). The community property bill was a compilation of what were perceived as the best parts of the community property laws of the existing community property states. The alternative bill would have retained Wisconsin's common law property system in a modified form. Neither bill passed.

In the 1983–84 legislative session, the same two bills (community property and modified common law) were again introduced. The community property proposal was 1983 Assembly Bill 200; the modified common law proposal was 1983 Assembly Bill 376. After its introduction, 1983 Assembly Bill 376 was amended to include a conventional (elective) community property system. The bill containing the conventional system was passed by the Wisconsin Assembly in October 1983 but was defeated in the Wisconsin Senate. In September 1983, the community property proposal, 1983 Assembly Bill 200, was amended to incorporate most of UMPA, which had been promulgated less than two months earlier. Assembly Bill 200 was passed by the state Senate in February 1984 and by the state Assembly in March 1984. It was signed into law on April 4, 1984, with an effective date of January 1, 1986.

A comprehensive trailer bill, clarifying the original law and making some additions, was enacted on October 22, 1985. The Act's original effective date, January 1, 1986, was not changed by the 1985 Trailer Bill. Since 1985, two other trailer bills have been passed, as discussed in section 1.2, *supra*. In addition, as discussed in section 1.2, *supra*, 1997 Wis. Act 188, revising the Probate Code, included revision to the former deferred marital property election against probate assets and the augmented marital property estate election against nonprobate assets, as discussed in section 1.2, *supra*.

## II. Basic Principles [§ 1.9]

### A. Introduction [§ 1.10]

In the Wisconsin Statutes table of contents, six chapters are labeled “The Family”:

Chapter 765	Marriage
Chapter 766	Property Rights of Married Persons; Marital Property
Chapter 767	Actions Affecting the Family
Chapter 768	Actions Abolished
Chapter 769	Uniform Interstate Family Support Act
Chapter 770	Domestic Partnership

Chapters 765, 767, and 768 were left substantially unchanged by the enactment of the Wisconsin Marital Property Act. (Chapters 769 and 770 were created after enactment of the Wisconsin Marital Property Act.) Chapter 766, however, was substantially changed.

Before the Act, chapter 766 was titled “Property Rights of Married Women.” It consisted of 12 sections providing that a woman's property was not subject to disposal by her husband, was not liable for his debts, and so forth. This was Wisconsin's version of the Married Women's Property Act. The Wisconsin Marital Property Act repealed and recreated chapter 766 so that, in effect, it is now a “Married Person's Property Act.”

Section 1.11, *infra*, sets forth the statutes describing the basic rights and duties of the spouses as created or modified by the Act.

## B. Basic Rights and Duties of Spouses [§ 1.11]

The Act created section 52.01(1m) (which was renumbered section 49.90(1m) and amended by 1985 Wisconsin Act 56), which provides the following: “Each spouse has an equal obligation to support the other spouse as provided in this chapter. Each parent has an equal obligation to support his or her minor children as provided in this chapter and chs. 48 and 49.”

Also, the Act amended section 765.001(2) by adding four sentences to it. Section 765.001(2) reads (additions are in italics):

**(2) Intent.** It is the intent of chs. 765 to 768 to promote the stability and best interests of marriage and the family. *It is the intent of the legislature to recognize the valuable contributions of both spouses during the marriage and at termination of the marriage by dissolution or death.* Marriage is the institution that is the foundation of the family and of society. Its stability is basic to morality and civilization, and of vital interest to society and the state. The consequences of the marriage contract are more significant to society than those of other contracts, and the public interest must be taken into account always. The seriousness of marriage makes adequate premarital counseling and education for family living highly desirable and courses thereon are urged upon all persons contemplating marriage. The impairment or dissolution of the marriage relation generally results in injury to the public wholly apart from the effect upon the parties immediately concerned. *Under the laws of this state, marriage is a legal relationship between 2 equal persons, a husband and wife, who owe to each other mutual responsibility and support. Each spouse has an equal obligation in accordance with his or her ability to contribute money or services or both which are necessary for the adequate support and maintenance of his or her minor children and of the other spouse. No spouse may be presumed primarily liable for support expenses under this subsection.*

Sections 49.90(1m), 765.001(2), and 767.501 (actions to compel support), together with the common law doctrine of necessities, define the spouses’ obligation to support each other and the means for enforcing that obligation. The duty of support is discussed in section 5.106, *infra*. The common law doctrine of necessities is discussed in section 5.107, *infra*.

The Act repealed all sections in chapter 766 except section 766.15 (the equal-rights section originally enacted in 1921). The Act created a new section 766.97. Section 766.97(1) is the old section 766.15 with

slight modifications. Section 766.97(2) restates in shortened form certain provisions of the previous version of chapter 766 that were repealed by the Act. Finally, the Act created section 766.97(3). Thus, section 766.97 as amended by the Act now reads:

**766.97 Equal rights; common law disabilities.** (1) Women and men have the same rights and privileges under the law in the exercise of suffrage, freedom of contract, choice of residence, jury service, holding office, holding and conveying property, care and custody of children and in all other respects. The various courts and executive and administrative officers shall construe the statutes so that words importing one gender extend and may be applied to either gender consistent with the manifest intent of the legislature. The courts and executive and administrative officers shall make all necessary rules and provisions to carry out the intent and purpose of this subsection.

(2) Nothing in this chapter revives the common law disabilities on a woman's right to own, manage, inherit, transfer or receive gifts of property in her own name, to enter into contracts in her own name or to institute civil actions in her own name. Except as otherwise provided in this chapter and in other sections of the statutes controlling marital property or property of spouses that is not marital property, either spouse has the right to own and exclusively manage his or her property that is not marital property, enter into contracts with 3rd parties or with his or her spouse, institute and defend civil actions in his or her name and maintain an action against his or her spouse for damages resulting from that spouse's intentional act or negligence.

(3) The common law rights of a spouse to compel the domestic and sexual services of the other spouse are abolished. Nothing in this subsection affects a spouse's common law right to consortium or society and companionship.

The Act also created other sections that describe the basic rights and duties of spouses. Section 766.15 provides:

**766.15 Responsibility between spouses.** (1) Each spouse shall act in good faith with respect to the other spouse in matters involving marital property or other property of the other spouse. This obligation may not be varied by a marital property agreement.

(2) Management and control by a spouse of that spouse's property that is not marital property in a manner that limits, diminishes or fails to produce income from that property does not violate sub. (1).

Section 766.17 provides:

**766.17 Variation by marital property agreement.** (1) Except as provided in ss. 766.15, 766.55(4m), 766.57(3) and 766.58(2), a marital property agreement may vary the effect of this chapter.

(2) Section 859.18(6) governs the effect of a marital property agreement upon property available for satisfaction of obligations after the death of a spouse.

Section 766.17 grants spouses considerable contractual freedom to vary the effect of the Act.

### **III. Constitutionality [§ 1.12]**

#### **A. Introduction [§ 1.13]**

A statute that changes property rights as dramatically as the Act may involve constitutional questions. Two provisions of the Act have generated interest because they affect important property rights that existed before the Act's effective date. The first provision involves income earned or accrued after the Act's effective date on pre-effective date property. The second provision involves deferred marital property rules. As yet there have been no published cases in which a party has challenged the constitutionality of any aspect of the Act. A long-standing acquiescence in the interpretation of a statute as constitutional may itself be given weight as a factor in determining its constitutionality. See, e.g., *Pocket Veto Case*, 279 U.S. 655 (1929); *State ex rel. Frederick v. Zimmerman*, 254 Wis. 600, 37 N.W.2d 473 (1949).

#### **B. General Statement of the Problem [§ 1.14]**

A legislative change in property rights as between spouses may be viewed as a taking from one spouse and a transfer to the other of a vested right to possess, use, enjoy, or dispose of property. If the statute is retroactive in nature, litigation questioning its constitutionality may result. An issue is whether a retroactive taking is either without due process of law or violates the Privileges and Immunities Clause of the 14th Amendment of the U.S. Constitution, or whether it is justified as within the police power of the state to regulate the marital relationship, the distribution of property at divorce, or the devolution of property at death. See, e.g., *Bouquet v. Bouquet*, 546 P.2d 1371 (Cal. 1976), and the discussion in section 1.17, *infra*.



### C. Income of Pre-Effective Date Property [§ 1.15]

Under the law that existed before the Act was passed, income accruing on property owned by a spouse was owned in full by that spouse as his or her separate property. The Act provides that income earned or accrued by a spouse during marriage and after the *determination date* (defined by section 766.01(5) as the last to occur of January 1, 1986, the date that both spouses are domiciled in Wisconsin, or the date of marriage) attributable to predetermination date property owned by that spouse (including property received by gift or inheritance during marriage and before the determination date and certain property acquired before marriage) is marital property. Wis. Stat. § 766.31(4). Under the Act, each spouse has a present, undivided one-half interest in marital property. Wis. Stat. § 766.31(3). The constitutional issue is whether the right to receive future income from property that is solely owned at the Act's effective date is a vested property right that the Act unconstitutionally took away. This question is considered generally before considering the impact of a unilateral statement under section 766.59.

➤ **Comment.** This discussion is confined to property owned at the Act's effective date. It is unclear whether the same considerations would apply to predetermination date property acquired after the effective date—for example, property acquired after January 1, 1986, and owned by a spouse residing in another jurisdiction who subsequently changes domicile to Wisconsin. *But see Garry v. Creswell (In re Estate of Thornton)*, 33 P.2d 1 (Cal. 1935).

The UMPA section 4 comment clearly anticipated the problem:

The income rule ... affects post-adoption income classifying it as marital property. Post-adoption income is just that. It is not principal, and it is received and regulated by the Act's provisions only when the claim of right to it occurs by virtue of its having been earned or accrued *after* adoption. Hence the Act's income rule is not retroactive.

The court in one case, *Willcox v. Penn Mutual Life Insurance Co.*, 55 A.2d 521 (Pa. 1947), used a different analysis. Shippen Lewis owned certain income-producing properties before his marriage to Mary Lewis and was also the recipient of income from a testamentary trust created for his benefit. After the parties' marriage but before enactment of federal legislation permitting joint income tax returns and before enactment of

the marital deduction, Pennsylvania adopted the Community Property Law of 1947, Act No. 550, 48 P.L. § 201, Pa. Laws (1947). The law was designed to give Pennsylvania residents income tax and estate tax benefits similar to those provided to residents of community property states. It provided that property acquired by either husband or wife during marriage and after the effective date of the law was community property, except property defined as separate property. These provisions were interpreted to mean that income generated on separate property and received after the effective date of the law would be community property. *Willcox*, 55 A.2d at 525.

Following enactment of the Pennsylvania Community Property Law, Mr. Lewis used income from his separate property and trust income to pay premiums on a life insurance policy. Mr. Lewis assigned the policy to Willcox. The insurance company refused to recognize the assignment on the ground that since the income used to pay premiums was community in nature, Mrs. Lewis's signature was required because she had an interest in the policy. A friendly lawsuit was commenced to determine whether Mrs. Lewis's signature was required.

Rather than using the analysis in the UMPA section 4 comment, the court held that there was a retroactive taking of one-half of the income involved. The court held that the right to future income was vested and was inherently part of the underlying property: "Of what value is it to an owner to be allowed to retain what would virtually be a mere nominal ownership, if he is compelled to surrender the profits and income therefrom?" *Id.* at 526.

The court then considered whether the taking was justified and elaborated on the legislature's power to regulate the spouses' property during and after termination of the marriage. The court held that the legislature could provide for the distribution of every person's property at death; could provide, to some extent, for the distribution of a married person's property at divorce; could establish an obligation of support during marriage; and could establish a community interest in a spouse's earnings (apparently meaning compensation) during a marriage. The court found it unconstitutional, however, to classify, as community property, income derived from property acquired before marriage and owned before the effective date of the state's community property law. According to the court, the legislature could regulate only those rights that arise wholly out of the marriage relation itself and could not transfer

from one spouse to the other “a property right which existed before, and entirely independently of, the marriage.” *Id.* at 527.

Federal legislation permitting joint income tax returns and the marital deduction for federal estate tax purposes, both adopted after passage of the Pennsylvania Community Property Law, obviated the law’s purpose. For these and other reasons, the court went on to invalidate the entire law.

The property right involved in *Willcox* existed before the marriage. It is unclear whether the reasoning of the *Willcox* decision would extend to income received by a spouse during marriage from property acquired during marriage by gift or inheritance on the theory that such income is also received “independently of the marriage.” Another issue is whether the court in *Willcox* would have reached the same result for income generated during marriage on solely owned property purchased during marriage, but before the effective date of the law, with compensation earned during the marriage on the ground that it arose out of marital effort.

A summary of the arguments and cases cited by the parties and in amicus curiae briefs filed in *Willcox* are found at Annotation, 174 A.L.R. 224 (1948). In addition, several law review articles, many of which are critical of the court’s reasoning, analyze the *Willcox* decision. *See, e.g.*, Jack Rowlett Lovell, Case Note, *Community Property—Constitutional Law—Due Process—Constitutionality of Pennsylvania Community Property Act of 1947*, 21 S. Cal. L. Rev. 383 (1948); Mary Stephenson, Note, *Community Property: Constitutionality of Oklahoma-Pennsylvania Community Property Law*, 1 Okla. L. Rev. 57 (1948).

In considering the constitutional propriety of the state’s attempt to redistribute ownership rights between spouses during a marriage, California’s experience with quasi-community property is also relevant. A review of this experience is found in W.S. McClanahan, *Community Property Law in the United States* 579–83 (1982).

In California, quasi-community property rules were adopted to solve a problem that occurs when spouses change domicile from a common law jurisdiction to a community property law jurisdiction. UMPA § 18 cmt. In a common law jurisdiction, the surviving spouse usually has the right to elect a share of the estate of the predeceasing spouse, often up to one third of that property. By changing domicile to a community

property law jurisdiction, however, the spouse loses the common law elective right because community property law jurisdictions do not provide an election against a predeceasing spouse's estate. *McClanahan, supra*, at 511. Quasi-community property rules provide that when spouses change domicile to a community property state, assets that would have been community property at their acquisition had the spouses then been domiciled in the community property state are treated as community property when the owner spouse dies. *See, e.g.*, Cal. Prob. Code §§ 66, 101, 102 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot).

Unlike the present California statutes, Cal. Fam. Code §§ 125, 2581, 2640 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot), which postpone quasi-community property treatment until the death or divorce of a spouse, the first version of California's quasi-community property law applied those rules immediately upon change of domicile. California Civil Code section 164 (1917) provided that property acquired while the spouses were domiciled elsewhere, which would not have been the separate property of either spouse if acquired while domiciled in California, became community property when the spouses moved to California. The 1917 statute was found unconstitutional under the Due Process and Privileges and Immunities Clauses of the 14th Amendment to the U.S. Constitution because the statute retroactively altered vested property rights upon change of domicile from a common law state to California in both *Garry*, 33 P.2d 1, and *Arms v. Heath (In re Estate of Arms)*, 186 Cal. 554, 199 P. 1053 (1921). In *Garry*, the assets involved were acquired during marriage (presumably with what would have been community property if California's statute had then applied to such assets) in a common law state, Montana, before the parties moved to California; thus, unlike in *Willcox*, the assets involved were apparently not acquired independently of the marriage.

The California Legislature's remedy to the constitutional problem was to revise the statute to postpone the applicability of the quasi-community property rules until the death (an event that involves the state's interest in devolution of property) of the owner (usually the titled) spouse. Cal. Civ. Code § 201.5 (Deering 1935). The California

Supreme Court indicated that this legislative change removed the constitutional problem. The court in *Kuchel v. Miller (In re Miller)*, 187 P.2d 722 (Cal. 1947), all but said that the revised statute was constitutional; in *Addison v. Addison*, 399 P.2d 897 (Cal. 1965), the court said that *Miller* did find the statute constitutional.

Arguably, by providing that postdetermination date income on predetermination date property is marital property, the Wisconsin Act's immediate transfer of ownership rights from one spouse to another at the Act's effective date has the same unconstitutional effect as California's 1917 legislation that transferred ownership rights from one spouse to another immediately upon change of domicile from a common law state to California. However, both the California Supreme Court and several commentators have questioned the reasoning of *Garry*. In *Addison*, a case applying quasi-community property rules at divorce, the court in dicta cited numerous commentators who have criticized the *Garry* decision and concluded by saying that the "correctness of the rule in [*Garry*] is open to challenge." 399 P.2d at 901. Subsequent commentary suggests that *Garry* would be overruled today. Barbara Brudno Gardner, *Marital Property and the Conflict of Laws: The Constitutionality of the Quasi-Community Legislation*, 54 Calif. L. Rev. 252, 266–67 (1966); Stephen M. Tennis, *Retroactive Application of California's Community Property Statutes*, 18 Stan. L. Rev. 514, 520 (1966). See also *Bouquet v. Bouquet*, 546 P.2d 1371 (Cal. 1976), in which the court declared that although *Addison* retroactively impaired vested property rights, it was still a proper exercise of the police power.

In Wisconsin, consideration should be given to whether the unilateral statement permitted by section 766.59 may obviate constitutional objections to this aspect of the Act. The unilateral statement, which classifies income from nonmarital property accruing after the effective date of the statement as individual property, permits a spouse to take affirmative action to avoid the result of the income rule in connection with predetermination date property otherwise mandated by section 766.31(4).

The unilateral statement, however, may not answer all constitutional challenges. An issue is whether a citizen and property owner may be required to take affirmative action, such as signing a unilateral statement, to retain property rights otherwise protected by the Constitution. Assuming that an affirmative action can be required, a constitutional

problem may still exist when a spouse is unable to execute a unilateral statement, perhaps, for example, because of incompetence.

Furthermore, a unilateral statement will not prevent all creditors from reaching the future income of property owned at the effective date of the Act. A creditor is not bound by a unilateral statement unless the creditor had actual knowledge of its provisions or a copy of the statement at or before extending credit. Wis. Stat. §§ 766.55(4m), .56(2)(c). A tort creditor, for instance, would almost never receive such notice, and to the extent that a tort creditor of one spouse could reach income from property owned at the effective date of the Act by the other spouse, a constitutional problem could arguably arise.

➤ **Comment.** This discussion need not be limited to tort creditors. An obligation incurred by one spouse after the determination date in the interest of the marriage or family may be satisfied from all marital property including the income stream of the nonincurring spouse. *See infra* ch. 5. If the nonincurring spouse executes a unilateral statement but for some good reason is unable to give notice of the unilateral statement to the creditor (and the creditor does not, in fact, have actual knowledge of the statement's provisions) before the obligation is incurred by the other spouse, postdetermination date income attributable to property of the nonincurring spouse acquired before the effective date of the Act is available to the creditor.

## **D. Deferred Marital Property [§ 1.16]**

### **1. United States Constitution [§ 1.17]**

Under the Act as originally adopted, certain assets owned by one spouse at the determination date constituted deferred marital property at that owner spouse's death if the other spouse survived and if the property would have been marital property if acquired after the determination date. Wis. Stat. § 851.055 (1995–96). As a consequence, that property was subject to elections under former sections 861.02 and 861.03. If, for example, in 1970, while both spouses are married and domiciled in Wisconsin, the husband purchased real estate with his salary, retained the real estate, and died domiciled in Wisconsin survived by his wife after December 31, 1985, deferred marital property concepts applied because at acquisition, the asset would have been marital property had the Act

been in effect. *See infra* ch. 12. Thus, at death the husband could, with certainty, dispose of only one-half of the real estate rather than all of it, since his wife (unless barred) could elect to take a one-half ownership interest in it. This approach was similar to the quasi-community property rules of California applicable to spouses who change domicile from a common law state to California. *See* Cal. Prob. Code §§ 66, 101, 102 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009–2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot); *see also* Idaho Code §§ 15-2-201 through -209 (West, WESTLAW current through (2010) Chs. 1-359 and HJR's 4, 5 and 7 that are effective on or before April 12, 2010).

As revised by 1997 Wisconsin Act 188, the deferred marital property election granted to a surviving spouse under chapter 861 is an election to take an *amount* equal to not more than one-half of the augmented deferred marital property estate. This is in contrast to the former probate election of deferred marital property, which allowed the surviving spouse to elect up to a one-half interest in each item of deferred marital property that was subject to administration. However, assets disposed of by a deceased spouse's will that constitute part of the augmented deferred marital property estate are available to satisfy the deferred marital property elective share. Wis. Stat. § 861.06. Thus, the deceased spouse's will disposes of each item of deferred marital property in accordance with the terms of the will, subject, however, to the possibility that the asset may be required to satisfy the deferred marital property elective share.

In *Addison*, 399 P.2d 897, California's similar quasi-community property rule was held constitutional at the divorce of a couple who had accumulated property in a common law state before changing domicile to California. (As to constitutionality of California's quasi-community property rules at death, see section 1.15, *supra*.) In its opinion, the court distinguished *Garry*, 33 P.2d 1, in which spouses who had acquired assets during their marriage in Montana with what would have been community property in California changed domicile from Montana to California, where one of them died. The *Addison* court said that property rights were not disturbed merely upon crossing the boundary into California; rather, they were being disturbed at a subsequent date—the date of divorce. The state's inherent police power provided the right to interfere with vested property rights in that circumstance because of the state's paramount interest in the equitable distribution of property owned

by spouses at divorce. This is true, said the court, even though *Garry* might be read as holding that legislation is unconstitutional if it impinges on a citizen's right to maintain a domicile in any chosen state without losing valuable property rights.

Arguably, *Addison* may be distinguished in connection with couples already living in a state when the law is changed. There is a voluntary aspect in making the decision to change domicile from one state to another and to subject oneself to a new set of laws. There may be an involuntary aspect for citizens already residing in Wisconsin at the Act's effective date if the only way to maintain existing property rights is to change domicile. (A marital property agreement is not an answer if one spouse refuses to participate.) However, in both instances, application of the law is deferred to a later date marking the occurrence of an event in which the state has an interest.

Various factors are relevant when considering the constitutionality of legislation that may retroactively impair vested property rights. Although it deals with an aspect of community property law that is not relevant here, *Bouquet*, 546 P.2d 1371, provides an excellent description of those factors.

The court in *Bouquet* noted that legislation that retroactively impairs vested property rights is not necessarily unconstitutional. In determining whether a retroactive law contravenes the Due Process Clause of the 14th Amendment of the U.S. Constitution, for example, a court should consider the significance of the state interest served by the law, the importance of retroactively applying the law to effect that interest, the extent of reliance on the former law, the legitimacy of that reliance, the extent of action taken on the basis of that reliance, and the extent to which retroactively applying the new law will disrupt those actions.

Thus, in constitutional litigation over the Act, courts will consider the fact that Wisconsin residents have relied on pre-Act law. Such reliance may involve various irrevocable transactions completed for estate planning purposes such as the making of gifts and the creation of irrevocable trusts. In addition, reliance on prior law may be significant in connection with record keeping. Many spouses, relying on the prior law in Wisconsin that title usually determined ownership, will not have sufficiently documented the source of acquisition of assets to trace assets that would not have been marital property at acquisition if the Act were then in effect. These assets may be reclassified to marital property



because of mixing, Wis. Stat. § 766.63(1), or because of the presumption that all property of spouses is marital property unless proven otherwise, Wis. Stat. § 766.31(2). Moreover, if it can be proved that an asset is not marital property, the asset is still subject to a second presumption that it is deferred marital property. Wis. Stat. § 858.01. Once again, record keeping, or the lack of it, is important.

In addition to describing the factors considered in constitutional litigation, *Bouquet* also puts *Addison* in perspective. In *Bouquet*, the court brushed aside statements in *Addison* that the quasi-community property rules were applied prospectively because they applied at death or divorce. In fact, the *Bouquet* court said that *Addison* retroactively impaired vested property rights but that such impairment was justified as a proper exercise of the police power.

Further support for the constitutionality of the deferred marital property rules may be found in cases in other jurisdictions that have upheld the creation of equitable distribution rules at dissolution of a marriage. Those cases affirm that such rules may affect not only property acquired after those statutes were enacted, but also property acquired before that. See, e.g., *Kujawinski v. Kujawinski*, 376 N.E.2d 1382 (Ill. 1978); *Fournier v. Fournier*, 376 A.2d 100 (Me. 1977); *Bacchetta v. Bacchetta*, 445 A.2d 1194 (Pa. 1982). *Fournier* distinguished *Willcox* on the basis that the equitable-distribution statute did not affect the ownership of property in any way in the absence of a separation or divorce.

A similar analysis may be used in connection with amendments to the Act made by 1993 Wisconsin Act 160, which state that the nonemployee spouse's marital property interest in IRA assets traceable to the rollover of a deferred-employment-benefit plan terminates at the nonemployee spouse's death if he or she predeceases the employee spouse. Arguably there is a taking of the nonemployee spouse's right to dispose at death of a marital property interest in the IRA that he or she previously had if he or she predeceases the employee spouse. The spouses may have made estate plans based on that right of disposition, but in some cases, it may not be possible to change those plans.

On the other hand, taking of the right to will does not injure the nonemployee spouse during his or her lifetime and may arguably be justified under the state's power to regulate marriages and dispositions at death in much the same way that the deferred marital property elections

may be justified. Moreover, the amendments simply extend the policy embodied in section 766.62(5), which provides a terminable interest in connection with deferred-employment-benefit plans so that those benefits are preserved in their entirety for a surviving employee spouse.

## 2. Wisconsin Constitution [§ 1.18]

Although the Wisconsin Court of Appeals has held that there is no right under the U.S. Constitution to dispose of property by will, *Eisenberg v. Eisenberg (In re Estate of Eisenberg)*, 90 Wis. 2d 620, 280 N.W.2d 359 (Ct. App. 1979) (citing *Demorest v. City Bank Farmers Trust Co.*, 321 U.S. 36 (1944)), a number of Wisconsin decisions hold that Wisconsin residents have that right under the Wisconsin constitution. *Biart v. First Nat'l Bank of Madison (In re Estate of Ogg)*, 262 Wis. 181, 54 N.W.2d 175 (1952); *Boehmer v. Kalk*, 155 Wis. 156, 144 N.W. 182 (1913); *Cowie v. Strohmeyer (In re Will of Rice)*, 150 Wis. 401, 136 N.W. 956 (1912). The holdings are based on article I, section 1 of the Wisconsin Constitution, which provides that “[a]ll people are born equally free and independent, and have certain rights; among these are life, liberty and the pursuit of happiness....”

The right to will, however, is subject to reasonable regulation by the legislature. Granting an elective right to take a share of a deceased spouse’s estate is a reasonable regulation of the inherent right to dispose of property by will. *Eisenberg*, 90 Wis. 2d 620. Arguably, the same is true of the elections provided a surviving spouse under former sections 861.02 and 861.03 and their successor provisions under current chapter 861, which were designed to replace the elective right in sections 861.01–.05 that was repealed by the Act.

It appears likely that a court in this state will hold that the elective rights under chapter 861 reasonably regulate devolution of property at death. Those elective rights protect a surviving spouse and promote “governmental encouragement of the marital relationship” (a phrase used in *Eisenberg*, 90 Wis. 2d at 629, in connection with the elective share only).

The deferred marital property election under chapter 861 is maximized because section 858.01 provides that if the presumption that all property of the spouses is marital property is overcome, a spouse’s remaining property at death is presumed to be deferred marital property.

Because previously there was no reason to keep the kinds of records that would be needed to rebut the presumption that nonmarital property of a spouse at death is deferred marital property, substantial property acquired before the determination date may (in the absence of records) fall into that category. Consequently, the elective rights under chapter 861 based on deferred marital property may reach as much as one-half the value of a decedent spouse's predetermination date property subject to administration or of the value of that property in nonprobate arrangements.

The elective right under chapter 861 may apparently be combined with the spousal allowance under section 861.35, which gives a court discretion to provide an allowance for a spouse (and set aside property for that purpose) for an indefinite period. Section 861.35 also allows the court to consider not only the means available for support but also the existing standard of living of the spouse applying for the allowance. But, in combination with elective right under section 861.02, the allowance could significantly diminish the right to will in a particular case and might exceed what would be considered reasonable regulation of that right.

Another constitutional challenge could arise in connection with the date used in the grandfather clause of former section 861.05(4), which exempted certain nonprobate arrangements from being included in the augmented marital property estate subject to election under former section 861.03 if the instruments involved were executed before April 4, 1984, the date the governor signed the original Act. The theory is that persons should have known on April 4, 1984, that deferred marital property rules would extend to nonprobate arrangements. See 1985 Trailer Bill Original Nontax Note to section 861.05(4). Actually, there was considerable doubt about that proposition as of April 4, 1984, and many amendments in the 1985 Trailer Bill, including adoption of the augmented estate concepts of the Uniform Probate Code, were required to achieve that result. If challenged, the constitutional issue may turn on whether nonprobate arrangements executed or amended after April 3, 1984 (and, arguably, before a date when notice of extension of deferred marital property rules to nonprobate arrangements was reasonably given), are accorded equal protection with those nonprobate arrangements executed or amended before April 4, 1984. See *Wisconsin Department of Revenue v. Trainer (In re Estate of Trainer)*, 123 Wis. 2d 102, 365 N.W.2d 893 (Ct. App. 1985), for discussion of a similar problem.

## **E. Other Matters [§ 1.19]**

Between 1983 and May 2010, the constitutionality of only two aspects of the Act has been considered. It may be anticipated that other provisions of the Act may be examined for constitutionality by the courts in the future.

## **IV. Trailer Bills [§ 1.20]**

The tables below summarize major changes made by the 1988 Trailer Bill and the 1992 Trailer Bill and indicate, when relevant, additional changes made by subsequent legislation.

**TABLE 1**

### **Summary of 1988 Trailer Bill**

1. Wis. Stat. § 857.03(2): Created a procedure permitting the surviving spouse and a beneficiary of the predeceasing spouse's estate to exchange interests in marital property. The trailer bill also changed Wisconsin tax statutes so that no gain or loss is recognized as a result of the exchange. Section 857.03(2) has since been amended and renumbered as section 766.31(3)(b)3.
2. Wis. Stat. § 766.01(8): Amended to provide that the Marital Property Act applies when both spouses are domiciled in Wisconsin. The term "marital domicile" was deleted from the Act. Other statutes were modified with respect to this clarification.
3. Wis. Stat. § 71.02(2)(me): Amended with respect to net rents and other net returns for income tax purposes. Section 71.02(2)(me) has since been amended and renumbered as section 71.01(16).
4. Wis. Stat. § 71.09(10m): Amended with respect to the apportionment of tax credits or refunds between spouses and former spouses. Section 71.09(10m) has since been amended and renumbered as section 71.75(8).
5. Wis. Stat. § 766.588: Created a statutory-form terminable marital property agreement (STMPCA) by which spouses may classify their existing and prospective assets as marital property. If there is no

financial disclosure, the agreement's duration is three years. If there is financial disclosure, the agreement's duration is unlimited and nonrenewable. In any event, the surviving spouse may make the deferred marital property and augmented marital property estate elections.

6. Wis. Stat. § 766.589: Created a statutory-form terminable marital property agreement (STIMPCA) by which spouses may classify all their assets as individual property, with certain exceptions.
7. Wis. Stat. § 766.01(9)(c), (d): Created to extend the definition of *held* to uncertificated securities and to a partner's interest in a general partnership.
8. Wis. Stat. § 766.31(10): Amended to provide that spouses may reclassify their property by a conveyance signed by both spouses. Section 766.605 was changed regarding the manner of holding homestead property, and sections 806.10(1) and 806.15(4) were changed regarding when a docketed judgment is a lien on real estate.
9. Wis. Stat. § 766.575: Amended to protect a trustee holding marital property when the trustee follows the instrument's terms in the absence of a notice of claim. The provisions are similar to changes made to section 766.61(2), which apply to issuers of life insurance policies (discussed below in item 11).
10. Wis. Stat. § 857.015: Amended to permit the "holding spouse" to direct in a will or other signed writing that the marital property interest of the "nonholding spouse" and any deferred marital property election be satisfied within one year of the decedent spouse's death from other property that is of equal clear market value at the time of satisfaction.
11. Wis. Stat. § 766.61: Amended to clarify the application of the Marital Property Act to life insurance insuring a spouse. For group insurance, the term *owner* is now defined as the holder of each individual certificate under the group plan. Also, the definition of policy was expanded for purposes of the written consent. Section 766.61(2) was completely rewritten and provides more detail as to when the issuer of a life insurance policy is and is not liable for acting in accordance with the terms of the policy. For group life insurance, the marital property classification rules remain in effect

even though the employer or other sponsor of the group policy changes carriers. Section 766.61(7) provides limitations on the remedy available when the noninsured spouse dies first. Section 766.61(8) clarifies that the life insurance rules do not apply to a life insurance policy held by a deferred-employment-benefit plan; instead, the rules for deferred-employment-benefit plans apply.

## **TABLE 2**

### **Summary of 1992 Trailer Bill**

1. Wis. Stat. ch. 71: Amended.
2. Wis. Stat. § 700.18: Amended to provide that persons who are named as owners in a document of title are tenants in common unless section 700.19 (joint tenancy) or chapter 766 (marital property) applies.
3. Wis. Stat. § 700.19(2): Amended to provide that when persons named as owners in a document of title are spouses who are not subject to the Marital Property Act (e.g., a couple domiciled in Illinois buys a cottage in Wisconsin), such persons are joint tenants in the absence of an expression of intent in the document of title. Generally, when there is no such expression of intent, the owners are tenants in common. Wis. Stat. § 700.18. The amendment applies to acquisitions after 1985. Note that since this change is retroactive, an issue may arise as to its constitutionality.
4. Wis. Stat. § 701.27(2)(bm): Created to provide that the surviving spouse may disclaim the decedent's interest in survivorship marital property. Section 701.27(2)(bm) has since been renumbered as section 701.26(1)(b).
5. Wis. Stat. § 766.31(10): Amended to expand the methods of reclassification to include an instrument that conveys an interest in a security, if the instrument is signed by both spouses.
6. Wis. Stat. §§ 766.58(3)(f), 767.266: Provided that will-substitute provisions in a marital property agreement are revoked upon dissolution of the marriage. Section 767.266 has since been amended and renumbered as section 767.375. Further, the new

provision extends beyond property subject to administration, making it clear that non-pro rata distributions are permissible for assets passing under any governing instrument.

7. Wis. Stat. § 766.58(7): Created to provide that the statutory terminable-interest rule continues to apply to deferred employment benefits classified as marital property by a marital property agreement unless the agreement provides otherwise and that the operation of section 766.61(7) (the *frozen interest rule*) is unaffected by a marital property agreement that classifies as marital property the noninsured spouse's interest in a policy that designates the other spouse as the owner and insured, unless the marital property agreement provides otherwise.
8. Wis. Stat. §§ 766.588(1)(d), .589(1)(c)1.: Created to provide that a statutory terminable marital property classification agreement (STMPCA) and a statutory terminable individual property classification agreement (STIPCA) do not affect the application of chapter 705 to joint accounts and marital accounts.
9. Wis. Stat. § 766.59(6): Created to permit a unilateral statement to be executed by persons intending to marry.
10. Wis. Stat. § 766.60(4)(b)1.: Amended to clarify that a marital property agreement may be used to create a joint tenancy between spouses who are otherwise subject to the Marital Property Act.
11. Wis. Stat. § 766.605: Amended to limit the creation-of-survivorship-marital-property rule to homesteads that are acquired in both spouses' names.
12. Wis. Stat. § 766.61(3)(e): Amended to correct an inconsistency in the definition of *ownership interest* for purposes of written consents regarding life insurance.
13. Wis. Stat. §§ 766.61(7), .70(6)(b): Amended to clarify and retain the frozen interest rule for marital property life insurance when the noninsured spouse dies first.
14. Wis. Stat. § 766.61(8): Amended to provide that a life insurance policy held by a deferred-employment-benefit plan is not life

insurance for purposes of the Marital Property Act. The policy is treated as part of a deferred employment benefit.

15. Wis. Stat. § 766.62(1)(b), (2): Amended to change the fraction applicable to deferred employee benefits so that the denominator is the period of employment giving rise to the benefit rather than the total period of employment.
16. Wis. Stat. § 766.63(1): Amended to provide that the mixing rule applies when marital property is mixed with other than marital property. The statute previously provided that the mixing rule applied when marital property assets were mixed with assets having another classification, which could arguably have been interpreted to exclude predetermination date property from the mixing rule.
17. Wis. Stat. § 806.15(5): Created to provide a procedure for removing a judgment lien that has attached to the real property of a nonobligated spouse acquired after the judgment is docketed.
18. Wis. Stat. § 815.205: Created to provide an exemption from execution in situations in which the docketed judgment becomes a lien on the real property interest of the nonobligated spouse when the interest was acquired after the judgment was docketed.
19. Wis. Stat. § 859.02(2)(a): Created to provide that a claim based on a marital property agreement is subject to the time limitations in section 766.58 (six months after filing of the inventory) and generally is not subject to the three-to-four-month period in the Probate Code.
20. Wis. Stat. § 859.18(6): Amended to clarify that a will-substitute provision does not adversely affect a creditor's rights.
21. Wis. Stat. § 861.02(1): Amended to provide that the surviving spouse's interest in elected deferred marital property in the probate estate is not subject to claims for funeral expenses or federal or Wisconsin estate taxes. This section has been repealed and replaced by section 861.05(3), which provides that the spouse's interest is subject to such claims.
22. Wis. Stat. § 861.02(1m): Created to provide that the surviving spouse may elect an interest in deferred marital property real estate



located in another state. There is a question whether the law of the other state will recognize this. The other state may apply Wisconsin law. This section has since been renumbered as section 861.02(2)(b).

23. Wis. Stat. § 861.05(3), (3)(b): Created new rules for determining the values of the spouses' interests in the augmented marital property estate. These subsections have since been amended and renumbered as subsections 861.05(2) and (2m).
24. Wis. Stat. § 861.07(3)(a): Amended to incorporate the actuarial tables used by the IRS to determine the value of life and term interests. Section 861.07 has since been repealed and recreated and no longer contains this provision.
25. Wis. Stat. §§ 861.31(4), .35(3): Amended to permit the probate court to charge the surviving spouse's allowances to the surviving spouse's shares of deferred marital property and the augmented marital property estate. Section 861.35(3) has since been renumbered as section 861.35(4).
26. Wis. Stat. § 861.33(1)(a)1.: Amended to provide that the surviving spouse's right of selection for wearing apparel and jewelry applies to items held for personal use by the decedent or the surviving spouse.
27. Wis. Stat. § 867.046(1) and (2): Clarified the summary confirmation procedures to remove the question whether they applied to survivorship marital property or will-substitute provisions.



## 2

# Classification of Property

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## I. Scope of Chapter [§ 2.1]

The comment to section 4 of the Uniform Marital Property Act (9A U.L.A. 103 (1998) [hereinafter UMPA], *reprinted in* app. A, *infra*) describes classification as “an essential process in applying” the uniform act. Classification plays the same essential role under the Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter

the Wisconsin Marital Property Act or the Act]; *see also infra* app. B (major legislation affecting the Act). The most important classification section of the Act is section 766.31. Section 766.31, with some significant exceptions, is based on section 4 of UMPA, which is described as the “heart” of UMPA. *See* UMPA § 4 cmt. Section 766.31 contains a general presumption, classification rules, and transitional rules. Other classification sections and associated rules are also important. This chapter defines and analyzes the basic classifications of property established by the Act, examines the definitions and presumptions on which the classifications are based, and reviews important associated rules.<sup>1</sup>

## II. Introduction [§ 2.2]

### A. Significance of Classification [§ 2.3]

Under the Wisconsin Act, classification of property has great significance in a variety of contexts. Examples include the following:

1. Classification determines rights of ownership.
2. Classification determines the applicability of the Act’s good-faith duty, *see* Wis. Stat. § 766.15. The good-faith duty applies to management and control by a spouse of marital property assets (and management and control by a spouse of the other spouse’s nonmarital property assets), but not to management and control by a spouse of his or her individual or predetermination date property.

➤ **Note.** With one exception, *see* Wis. Stat. § 766.31(6), predetermination date property is generally acquired before the Act applies to it. *See infra* §§ 2.8 (defining the term determination date), .141 (defining the term predetermination date property).

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189; all references to the United States Code (U.S.C.) and Internal Revenue Code (I.R.C.) are current through Pub. Law No. 111-154 (excluding Pub. L. Nos. 111-148, 111-152) (Mar. 31, 2010); and all references to the Treasury Regulations are current through 75 Fed. Reg. 17,023 (Apr. 2, 2010). Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

3. Classification may determine which assets are available to creditors, *see* Wis. Stat. § 766.55(2). For example, if an obligation in the interest of the marriage or the family is incurred by one spouse after the determination date, the creditor may reach all assets classified as marital property to satisfy the debt but generally may not reach the assets classified as nonmarital property of the nonincurring spouse.
4. Classification determines the quantum of an asset that may be freely disposed of by gift or at death. For example, only the one-half interest of a spouse in each item of marital property may be freely disposed of by that spouse at death; on the other hand, in most cases, each item of individual property of a spouse may be freely disposed of by that spouse at death.
5. Classification may have tax consequences. All assets classified as marital property, even that interest owned by a surviving spouse, will, as community property, obtain a basis adjustment at death under I.R.C. § 1014(b)(6). By contrast, such a change in basis is not accorded assets classified as nonmarital property of the surviving spouse.

## **B. Universal Marital Property Not Adopted [§ 2.4]**

Theoretically, it would have been possible to adopt a universal marital property regime in which all property possessed by spouses, including property either acquired by gift or inheritance or owned at the marriage, would be classified as marital property. This regime was not adopted in Wisconsin. Instead, a system was established that recognizes various classifications of property similar to those found in other U.S. community property jurisdictions.

Based on Spanish and to some extent French antecedents, the community property systems established in other U.S. community property jurisdictions are thought of as recognizing marriage as an equal partnership between husband and wife. *See* W.S. McClanahan, *Community Property Law in the United States* 331–32 (1982). The eight other community property states are Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, and Washington. Puerto Rico is also a community property jurisdiction. Historically, property brought to the marriage remained the separate property of the owning spouse throughout the marriage. In addition, property acquired by either spouse

during marriage by so-called lucrative title, usually defined as property received without consideration, remained that spouse's separate property. Other property acquired during the marriage in exchange for labor, effort, skill, money, or community assets was thought of as property acquired by so-called onerous title, and that property was known as community property. McClanahan, *supra*. Many of the same basic principles pertain in the other community property states today.

### **C. Reclassification of Property [§ 2.5]**

The Act establishes a classification system governing the property of spouses domiciled in Wisconsin. However, the Act also provides spouses with the means to vary the Act's effect. Thus, with certain limited exceptions (relating to the good-faith duty, the protection of certain third parties, and the support of dependent children), spouses may create their own classification system or reclassify their property by marital property agreement. Wis. Stat. § 766.17(1); *see infra* § 2.284, ch. 7. In addition, property of a spouse or spouses may be reclassified in a variety of other circumstances. *See infra* §§ 2.283–.295.

Listed below are some of the ways property of a spouse or spouses may be reclassified, other than by marital property agreement. By its nature, the list is general and cannot give the detail found in sections 2.283–.295, *infra*, and other sections and chapters of this book.

1. A spouse or spouses may reclassify property by gift, *see infra* §§ 2.285–.288, real estate by conveyance, *see infra* §§ 2.285–.288, and life insurance policies and premiums on those policies by written consent, *see infra* § 2.290.
2. A spouse may classify income from nonmarital property by unilateral statement. *See infra* § 2.289.
3. A spouse or spouses may reclassify property by attempting to create a joint tenancy or tenancy in common exclusively between spouses after the determination date, *see infra* § 2.293, or by using property to acquire a homestead exclusively between spouses after the determination date, *see infra* § 2.294.

4. A spouse or spouses may reclassify property by decree, *see infra* § 2.291, and by mixing property of different classifications to such an extent that tracing is of no assistance, *see infra* § 2.292.

### III. Overview of Classification System [§ 2.6]

#### A. In General [§ 2.7]

Before considering property classifications in detail, a key term—*determination date*—must be defined. The definition provided in section 2.8, *infra*, is followed by a brief overview of the classification system and several associated rules.

#### B. Determination Date and During Marriage Defined [§ 2.8]

Wisconsin was a common law state that converted to a community property (albeit labeled marital property) system. *See* Wis. Stat. § 766.001(2). The Act's effective date was January 1, 1986. The marital property regime applies to married couples at the determination date, a term defined in section 766.01(5) as follows:

“Determination date” means the last to occur of the following:

- (a) Marriage.
- (b) 12:01 a.m. on the date that both spouses are domiciled in this state.
- (c) 12:01 a.m. on January 1, 1986.

➤ **Note on Terminology.** The term *during marriage* as used in this chapter should be understood to mean “during marriage as defined by the Act.” On occasion, the Act uses the phrase “during marriage and after the determination date.” *See, e.g.,* Wis. Stat. § 766.31(4). In view of the definition of during marriage, the words “and after the determination date” are redundant. Nevertheless, this chapter uses the longer phrase when dealing with sections of the Act that also use it.

Section 766.03 explains when the Act first applies to spouses, when it ceases to apply, and what consequences flow from those events. Thus, chapter 766 first applies to spouses upon their determination date, except as provided in subsections 766.58(5), (11), and (12) and section 766.585



(all dealing with the effect of certain marital property agreements) and except for the application of section 766.97 (dealing with certain civil rights of spouses). After the Act first applies to spouses, it continues to apply during marriage. Section 766.75 applies after dissolution. If at the time of a spouse's death, both spouses are domiciled in Wisconsin, the chapter 766 provisions applicable after the death of a spouse apply.

The Act ceases to apply when one or both of the spouses are no longer domiciled in Wisconsin. *See* Wis. Stat. § 766.03(3) (Act applies to spouses "during marriage"). However, the cessation of the application of chapter 766 because a spouse is no longer domiciled in Wisconsin does not by itself affect any property, right, interest, or remedy acquired under chapter 766 by either spouse or by a third party. Wis. Stat. § 766.03(3). Nor does it affect by itself the satisfaction of any obligation incurred by a spouse under chapter 766 while both spouses were domiciled in Wisconsin. Wis. Stat. § 766.03(5). For a discussion of rights that may have accrued while only one spouse was domiciled in Wisconsin after January 1, 1986, and before the effective date of the 1988 Trailer Bill, see the discussion at section 13.46, *infra*.

January 1, 1986, is the determination date for spouses who were both domiciled in Wisconsin at that time. For spouses who both establish domicile in Wisconsin after January 1, 1986, their determination date is the date that both spouses establish domicile in this state. For persons who are both domiciled in Wisconsin and who marry after January 1, 1986, their determination date is the date of their marriage. Spouses may have more than one determination date.

➤ **Example.** Assume that a married couple is domiciled in Wisconsin on January 1, 1986, but on January 1, 1988, one of the spouses changes domicile to a common law state and then on January 1, 1991, changes domicile back to Wisconsin. The spouses may have accumulated marital property from January 1, 1986, to January 1, 1988, and could again accumulate marital property on and after January 1, 1991. Deferred marital property could have been accumulated from the date of marriage to January 1, 1986, and from January 1, 1988, to January 1, 1991.

The determination date for most spouses will be the date of their marriage. It should be noted that when both spouses are domiciled in Wisconsin at the date of their marriage and their marriage occurs after January 1, 1986, the property owned by a spouse at the date of the

marriage is that spouse's individual property. Wis. Stat. § 766.31(6); *see infra* § 2.12. The Act does not classify property owned by either or both of the spouses at a determination date that is either January 1, 1986, or the date when both spouses first become domiciled in Wisconsin. That unclassified property is referred to in this book as *predetermination date property*. Each item of predetermination date property has its own characteristics determined by predetermination date law as modified by the Act. *See infra* §§ 2.140–.154. Property acquired by spouses after the determination date (from sources other than those traceable to predetermination date property) is marital or individual property, depending on factors considered later in this chapter.

## **C. Basic Classifications [§ 2.9]**

### **1. Marital Property [§ 2.10]**

Generally, marital property consists of wealth created by a spouse's efforts as well as income earned or accrued from a spouse's property during a marriage and after the determination date. Each item of marital property is owned in present undivided one-half interests by the spouses. Wis. Stat. § 766.31(3). All property of spouses is presumed to be marital property and is so classified unless proven to be classified otherwise. Wis. Stat. § 766.31(1), (2); *see infra* § 2.26.

### **2. Terminable-interest Marital Property [§ 2.11]**

The marital property interest of a spouse in the other spouse's deferred-employment-benefit plan may be terminable. Thus, the nonemployee spouse's marital property interest in the employee spouse's deferred-employment-benefit plan terminates if the nonemployee spouse predeceases the employee spouse. Wis. Stat. §§ 766.31(3), .62(5); *see infra* § 2.201. A similar rule applies in connection with the augmented deferred marital property election, *see* § 2.243, *infra*.

Certain personal-injury recoveries have attributes similar to terminable interest property as far as the uninjured spouse is concerned. *See* Wis. Stat. § 766.31(7m); *see infra* § 2.133.

A terminable-interest rule also applies to certain rights under a life insurance policy when the surviving spouse is the owner and the insured. Wis. Stat. § 766.61(7); *see infra* § 2.178.

Assets in an individual retirement account (IRA) traceable to the marital property component of a rollover of a deferred-employment-benefit plan are terminable-interest marital property. Wis. Stat. § 766.62(5)(b), .31(3); *see infra* § 2.202.

### **3. Individual Property [§ 2.12]**

After the determination date, individual property assets may exist along with marital property assets. The comment to UMPA section 4 says that an item of individual property, except for its income, is analogous to an item of solely owned property in the common law system. Individual property consists primarily of:

1. Assets owned by a spouse at a marriage taking place after January 1, 1986, if both spouses, at the date of marriage, have a Wisconsin domicile, Wis. Stat. § 766.31(6);
2. Assets acquired by a spouse during marriage and after the determination date by gift or inheritance or that become the spouse's individual property by being classified as such by a marital property agreement, Wis. Stat. § 766.31(7)(a), (d); and
3. Assets acquired by a court decree that classifies the assets as a spouse's individual property, Wis. Stat. § 766.31(7)(d).

Appreciation of an individual property asset after the determination date and during marriage is also classified as individual property unless the appreciation is substantial and results from a spouse's substantial undercompensated efforts. *See* Wis. Stat. § 766.63(2). However, income earned or accrued by a spouse during marriage and after the determination date and attributable to individual property is classified as marital property unless such income is (1) classified as individual property by a unilateral statement under section 766.59, (2) reclassified by a marital property agreement or court decree, or (3) received as a gift from the other spouse. Wis. Stat. § 766.31(4), (10); *see infra* §§ 2.106–.121. As to income distributed to one spouse from a trust created by a third party, see section 766.31(7)(a) and section 2.84, *infra*.

#### 4. Predetermination Date Property [§ 2.13]

Property owned by spouses at a determination date that is either January 1, 1986, or the date when both spouses first are domiciled in Wisconsin is referred to in this book as predetermination date property, although the Act does not use this term. Such property is sometimes referred to as *unclassified property*. Note that property owned by a spouse at a marriage occurring on or after January 1, 1986, when at the date of the marriage both spouses are domiciled in Wisconsin, is individual property, not predetermination date property. *See supra* § 2.12. Each item of predetermination date property has its own characteristics determined under predetermination date law as modified by the Act. *See infra* §§ 2.140–.154.

The conclusions expressed in this section are confirmed by clarifying amendments to subparts 766.31(6)(a) and (b) in sections 46 and 47 of 2005 Wisconsin Act 216. The amendments state that if the date of the marriage is the same as the determination date, the property owned by a spouse at the determination date is that spouse's individual property. On the other hand, if the date of marriage precedes the determination date (as for example, a marriage in a common law state before both spouses change domicile to Wisconsin), the property owned by a spouse at the determination date is unclassified property (or what this chapter refers to as predetermination date property).

#### 5. Mixed Property [§ 2.14]

On occasion, marital property assets may be mixed with nonmarital property assets (for example, if marital property cash and individual property cash are both used to purchase an asset), which produces a mixed asset. An important rule associated with the classification process is that if the nonmarital component can be traced, it remains nonmarital property; if the nonmarital component cannot be traced, the entire asset becomes marital property. Wis. Stat. § 766.63(1); *see infra* ch. 3 (especially chapter 3, part III). Mixing and tracing rules may also be important in connection with the deferred marital property election. *See infra* § 3.4. Life insurance policies and deferred-employment-benefit plans are often special types of mixed property and are given special treatment under the Act. *See* Wis. Stat. §§ 766.61, .62; *see also infra* §§ 2.156–.219.

## 6. Deferred Marital Property [§ 2.15]

Predetermination date property is also deferred marital property if it would have been marital property under chapter 766 if acquired while the Act was in effect. Wis. Stat. § 851.055. Whether deferred marital property exists is considered only at death, and then only in the context of the deferred marital property election provided a surviving spouse. *See* Wis. Stat. §§ 861.02, .03.

The deferred marital property election is available to the surviving spouse only. It is not available to the estate of the first spouse to die. Thus, if a spouse owning or retaining certain interests in deferred marital property assets dies survived by the other spouse, the surviving spouse may have a right of election with respect to the assets' value. The election pertains to deferred marital property assets that make up the augmented deferred marital property estate. *See* Wis. Stat. §§ 861.02, .03; *see also infra* §§ 2.220–.246, ch. 12.

➤ **Note.** A grandfather provision in connection with certain arrangements made before April 4, 1984, was *repealed by* 1997 Wisconsin Act 188. *See* Wis. Stat. § 861.05(4) (1995–96), repealed by 1997 Wis. Act 188, § 194.

An exception to the above occurs if the deceased spouse was murdered by the surviving spouse. *See* § 2.226, *infra*.

A deceased spouse's assets are presumed to be deferred marital property to the extent the presumption that all property of spouses is marital property is rebutted. *See* Wis. Stat. § 861.02(2)(a); *see also infra* §§ 2.220–.246, 12.136–.147 (more detailed discussion of deferred marital property).

## IV. Marital Property [§ 2.16]

### A. Definition [§ 2.17]

Generally, marital property consists of (1) property accumulated during marriage and after the determination date by either or both of the spouses through a spouse's efforts, (2) income earned or accrued from a spouse's property during marriage and after the determination date, or

(3) property reclassified from nonmarital property to marital property by some means provided by the Act. Exceptions to this definition will be noted.

## **B. Attributes [§ 2.18]**

### **1. Necessity of Property [§ 2.19]**

Only property of spouses can be marital property; thus, marital property must first be property. A mere expectancy is not property. *See infra* § 5.23. Similarly, property titled in a trustee spouse who holds the property for a beneficiary of a trust created by a third person does not constitute property of the trustee spouse. *Leslie v. Midgate Ctr., Inc.*, 436 P.2d 201 (Wash. 1967); *see also* William A. Reppy Jr. & Cynthia A. Samuel, *Community Property in the United States* 202 (2d ed. 1982). The Act broadly defines the word *property* to include “an interest present or future, legal or equitable, vested or contingent, in real or personal property.” Wis. Stat. § 766.01(15). This broad definition includes contract rights, *see infra* §§ 2.274–.277, and beneficial interests such as interests in trusts, *see infra* §§ 2.272, 2.100.

### **2. Necessity of Marriage [§ 2.20]**

Because marital property assets may be owned only by spouses, *see* Wis. Stat. § 766.31(1), an asset may not be classified as marital property unless there is first a marriage between a man and a woman. *See* Wis. Stat. § 765.001(2). The Act is concerned with the property of married persons, and if a man and a woman are not married, the property they own is not marital property. UMPA § 1(8) cmt. In support of this concept (and that of the determination date), the term during marriage is defined in section 766.01(8) to mean a period in which both spouses are domiciled in this state, beginning at their determination date and ending at dissolution or at the death of a spouse. Section 766.03 establishes that the Act ceases to apply on the date only one spouse is domiciled in this state. Because the period when certain property is marital property is during marriage, and because the Act’s provisions addressed to “spouses” only apply for that period, UMPA § 1(8) cmt., the definition of marriage is important.

➤ **Note.** Section 765.001(2), which applies to chapters 765 to 768 (the Family Code), states: “Under the laws of this state, marriage is a legal relationship between 2 equal persons, a husband and wife, who owe to each other mutual responsibility and support.” This language precludes the creation of marital property between persons who cohabit and precludes marriages of persons of the same sex. *See also* Wis. Const. art. XIII, § 13 (stating that only marriage between one man and one woman is considered valid or recognized as marriage by state of Wisconsin).

If a marriage is invalidated by a decree, section 766.73 authorizes a court to apply as much of chapter 766 to the property of the parties to the invalid marriage as is necessary to avoid an inequitable result. Section 766.73 by its terms does not apply if section 767.61 applies to the action to invalidate the marriage and divide the property.

➤ **Comment.** A subject for speculation is whether Wisconsin courts will follow the rules developed in some community property states, such as Washington, dealing with invalid marriages when one or both of the spouses have acted in bad faith. *See* Harry M. Cross, *The Community Property Law in Washington (Revised 1985)*, 61 Wash. L. Rev. 13, 21–27 (1986); *see also infra* ch. 11 (putative spouses and definitions of marriage).

### 3. Present Undivided One-half Interest [§ 2.21]

Section 766.31(3) provides that “[e]ach spouse has a present undivided one-half interest in each item of marital property.” A spouse’s interest vests on acquisition, in contrast to an expectancy that ripens into a vested property interest on some later occurrence such as death or dissolution.

The comment to UMPA section 4 states that marital property “is created *as assets are acquired* by the spouses whether from income from the effort of either spouse during marriage, as income attributable to passive or investment sources, or as appreciation of or in exchange for or rollover of existing marital property.” The incidents and attributes of marital property, including the creation of a present legal interest, attach when the property is acquired. An item’s classification as marital property persists until the marriage terminates by dissolution or death, or

until the property is reclassified by one of the methods provided in the Act.

#### 4. Item-by-item System [§ 2.22]

The present undivided one-half interest that each spouse has in marital property, *see supra* § 2.21, means that each spouse owns one-half of *each* item of marital property, rather than one-half of the aggregate of all marital property. Wis. Stat. § 766.31(3). Upon either spouse's death, the surviving spouse retains his or her undivided one-half interest in each item of marital property. Wis. Stat. § 861.01(1). If a third party then succeeds to all or part of the decedent's one-half interest in an asset classified as marital property, that party becomes a tenant in common with the surviving spouse. Wis. Stat. § 861.01(2). For a discussion of the estate planning consequences of an item-by-item system, see chapter 10, *infra*.

➤ **Note.** The item-by-item rule apparently applies in all community property states. Arizona is perhaps the only state that applies the aggregate rule at death. Reppy & Samuel, *supra* § 2.19, at 314.

After dissolution, each former spouse owns an undivided one-half interest in each former marital property asset as a tenant in common, unless the decree or an agreement entered into by the spouses specifies otherwise. Wis. Stat. § 766.75. However, the item-by-item system is not relevant at dissolution. Thus, a decree could award marital property asset *A* to the wife and marital property asset *B* to the husband, consistent with equitable distribution under section 767.61.

The rules of management and control set forth in section 766.51 and described in chapter 4, *infra*, may in certain cases limit a spouse's right to claim an individual interest in a specific item of marital property. Thus, a spouse with sole management and control may subject assets to buy-sell arrangements. *See infra* § 4.81. In addition, sections 766.51(10), 857.015, and 861.015 permit a spouse who holds a marital property business interest described in subsection 766.70(3)(a), (b), or (d), which is not also held by the other spouse, to direct in a will or other signed writing that the nonholding spouse's marital property interest may be satisfied from other property at death. For further discussion of this aspect of management and control, see sections 4.83 and 12.36, *infra*.



During marriage, each spouse owns a one-half interest in each item of marital property. However, the right to manage and control an asset classified as marital property is an important matter requiring separate discussion. *See* Wis. Stat. § 766.51; *see also infra* ch. 4. Spouses must observe certain duties in connection with assets classified as marital property. *See infra* ch. 8. There are also rules and remedies (provided in certain cases) in connection with gifts of assets classified as marital property. *See* Wis. Stat. § 766.53; *see also infra* chs. 8 (remedies), 5 (credit), 6 (collection).

➤ **Note.** The Real Property, Probate and Trust Law section of the State Bar of Wisconsin formed a Probate Code “Trailer Bill” Drafting Committee that published “Notes to 2005 Wis. Act 216,” *available at* <http://www.wisbar.org/AM/Template.cfm?Template=/CM/ContentDisplay.cfm&ContentID=57842>. References in this chapter to “Committee Note(s)” are references to this document.

The item-by-item system can also be altered by agreement. 2005 Wisconsin Act 216 created subsection 766.31(3)(b), which permits spouses to provide in a marital property agreement that, upon the death of one spouse, some or all of their marital property may be divided between them based on aggregate value rather than item by item. In addition, a surviving spouse and the successor in interest to the decedent’s share of the marital property may enter into an agreement providing that some or all of the marital property in which each has an interest will be divided based on aggregate value rather than item by item. A *successor in interest* includes any person or entity that succeeds to the marital property interest of the deceased spouse, such as a personal representative, a trustee, or the beneficiary of a nonprobate transfer. Committee Note to section 42. The definition does not include a beneficiary under a will or trust. If the surviving spouse dies before the estate of the first spouse to die is fully administered, an agreement may be reached by the two successors in interest. In the absence of an agreement like any of those described above, the item-by-item system applies.

Former section 857.03(2) is now amended and renumbered as section 766.31(3)(b)3. and (intro.). *See* 2005 Wis. Act 216, § 169. The renumbered and amended section essentially coordinates with the amendments described above. Thus, it provides that a surviving spouse and a distributee who is a successor in interest to all or part of a deceased spouse’s interest in marital property may petition the court to approve an

exchange of interests in the marital property authorized by an agreement described above, but court approval of the exchange is not required for the agreement to be effective. If the court approves the exchange, the surviving spouse and the distributee must exchange their respective interests in two or more items of marital property. The exchange must occur before final distribution of assets under the governing instrument.

A court is allowed to approve the division of both nonprobate property and probate property. Committee Note to section 169. It appears that court approval of the division of nonprobate property is not required but may be sought if it is desirable.

➤ **Note.** The right to make exchanges may be a postmortem planning tool in some cases. *See infra* ch. 10.

## 5. Prohibition of Unilateral Severance [§ 2.23]

Under a marital property regime, a spouse may not unilaterally alienate his or her interest in any assets classified as marital property, receive the proceeds as his or her individual property, and then substitute the purchaser as a tenant in common with his or her spouse. The Act does not specifically address this matter, but one authority states that in community property jurisdictions, such a transaction is prohibited by either statute or case law. *See* Reppy & Samuel, *supra* § 2.19, at 20.

A spouse's unilateral attempt to sever his or her marital property interest in a marital property asset is, in effect, an attempt to reclassify the interest. Such an attempt will fail. The only means of reclassification available to spouses are the means provided by the Act, examples being interspousal gifts and marital property agreements; no provision is made for unilateral severance of a marital property interest in an asset. *See infra* §§ 2.283–.295 (reclassification methods). Unless the spouses reclassify their property by a means provided by the Act, all their property (including sale proceeds) is marital property except that which is classified otherwise under chapter 766. Wis. Stat. § 766.31(1).

Thus, even though a spouse may have management and control rights and could sell or exchange all or a portion of a marital property asset, each spouse has a marital property interest in the proceeds received from the sale or the property received in the exchange, as well as in any portion of the asset retained.

Courts have analogized community property to various common law property arrangements. For example, community property is sometimes thought of as partnership property, and analogies are made to partnership law. *See, e.g., Fink v. United States*, 454 F.2d 1387 (Ct. Cl. 1972). The UMPA prefatory note speaks of a “sharing ideal” in which “ownership of all of the economic rewards from the personal effort of each spouse during marriage is shared by the spouses in vested, present, and equal interests.” Despite these analogies, marriage is not a partnership in the technical legal sense of either chapter 178 or the Internal Revenue Code, and marital property is unlike anything in the common law system. Marital property interests are present undivided one-half interests without regard to the actual monetary value of a spouse’s contribution or any intent to make a profit. Moreover, a partner may convey his or her interest in a partnership to a third party, whereas a spouse may not convey his or her interest in a marital property asset as a separate interest. *See also* Michael J. Vaughn, *The Policy of Community Property and Inter-Spousal Transactions*, 19 Baylor L. Rev. 20, 28 (1967).

## **C. Basic Rule and Basic Presumptions [§ 2.24]**

### **1. Basic Rule [§ 2.25]**

Section 766.31(1) states that “[a]ll property of spouses is marital property except that which is classified otherwise by this chapter and that which is described in sub. (8).” The reference to section 766.31(8) specifically picks up predetermination date property. This broad rule is typical of most community property states. McClanahan, *supra* § 2.4, at 333. It is important to understand that the rule is not stated in terms of property acquired during marriage. Instead, *all property of spouses* is marital property, regardless of the time, method, or source of acquisition, unless it can be proven that the property is classified otherwise by chapter 766. (Thus, marital property can include assets wrongfully acquired by conversion or illegal contract. *See* McClanahan, *supra* § 2.4, at 334.)

### **2. Basic Presumptions [§ 2.26]**

Supporting the general rule in section 766.31(1), *see supra* § 2.25, is the basic presumption stated in section 766.31(2) that “[a]ll property of spouses is presumed to be marital property.” The presumption assumes

the existence of property and the appropriate marital relationship. *See supra* §§ 2.19, .20. If property and the appropriate marital relationship exist, then the presumption acts in a very broad manner. Making no reference to time, method, or source of acquisition, the presumption applies to “all property of spouses.” For example, an asset might have been inherited by a spouse during marriage and after the determination date. Such an asset is individual property if proof to that effect is sufficient to rebut the presumption favorable to marital property. Absent that proof, the presumption prevails, and the asset is marital property. Along these same lines, the comment to UMPA section 4 states that “[t]he bias of the presumption favors classifying spousal assets as marital property. Thus at the beginning of any process of classifying spousal assets, *everything* is presumed to be marital property” (emphasis added).

➤ **Note.** Four types of presumptions with similar purposes have been identified in community property states, some more favorable to the community than others. The Wisconsin presumption, which has been characterized as the *possession formula*, is quite favorable to the community (marital property) and is closest to the presumption in Arizona, Louisiana Texas, and Washington. *See* Reppy & Samuel, *supra* § 2.19, at 53–54.

The Act also establishes that if the presumption in section 766.31(2) is overcome, the property is presumed to be deferred marital property at death. Wis. Stat. § 861.02(2)(a). If at the death of a spouse the presumptions under sections 766.31(2) and 861.02(2)(a) are both overcome, the property is classified as nonmarital property that is not deferred marital property.

## D. Rebutting Presumptions [§ 2.27]

### 1. In General [§ 2.28]

A spouse may rebut the basic presumption under section 766.31(2) favorable to the classification as marital property by proving that the nonexistence of such a classification is more probable than its existence. *See* Wis. Stat. § 903.01. The burden of persuasion is on the proponent of nonmarital property classification. If adequate proof is presented to overcome the general presumption, the proponent of a nonmarital property classification prevails. UMPA § 4 cmt.; *see Malnar v. Stimac*

(*In re Estate of Malnar*), 73 Wis. 2d 192, 243 N.W.2d 435 (1976) (application of section 903.01 in different context).

The presumption under section 861.02(2)(a) can be rebutted in the same fashion. Evidence sufficient to rebut the first presumption may be sufficient to rebut the second. Wis. Stat. Ann. § 858.01(2) Legis. Council Notes—1985 Act 37, § 166 (West 2002) (current version of statute at 861.02(2)(a)).

➤ **Note.** In the other community property states, the evidence needed to rebut the presumption favoring the community usually must meet one of two tests: the “clear and convincing” test (Arizona and Texas) or the “mere preponderance of the evidence” test (New Mexico). See Reppy & Samuel, *supra* § 2.19, at 55. Decisions in some of the other community property states are in conflict over which of the two tests should apply. *Id.*

For two cases that apply the presumptions and the rules of burden of proof, see *Estate of Kobylski v. Hellstern* (*In re Estate of Kobylski*), 178 Wis. 2d 158, 503 N.W.2d 369 (Ct. App. 1993), and *Lloyd v. Lloyd* (*In re Estate of Lloyd*), 170 Wis. 2d 240, 487 N.W.2d 647 (Ct. App. 1992). See also *infra* § 3.48.

## 2. Effect of Title and Management and Control

### [§ 2.29]

When dealing with common law property, lawyers are accustomed to looking at title as the equivalent of ownership. Under a marital property regime, however, title is not synonymous with ownership, and proof that title to an asset is in one spouse or the other will not rebut the basic presumption that a spouse’s property is marital property.

Assume, for example, that a husband after the determination date purchases real estate with his salary (a marital property asset) and takes title in his name. Unless there is a marital property agreement or sufficient evidence of a gift by the wife, the asset is marital property. In the classification process, “[t]itle is *not* an answer since title functions ... principally to establish management and control rights.” UMPA § 4 cmt.; see also *infra* ch. 4. Consistent with this principle, the right to

manage and control property neither determines classification nor rebuts the presumption favorable to marital property. Wis. Stat. § 766.51(5).

Some caveats must be noted. First, title may establish classification in a limited number of situations. If, for example, a document of title, instrument of transfer, or bill of sale expresses an intent to establish a joint tenancy or tenancy in common exclusively between spouses after the determination date, the property is survivorship marital property or marital property, respectively. Wis. Stat. § 766.60(4)(b)1.a., b. In addition, a homestead acquired after the determination date exclusively between spouses is survivorship marital property if no contrary intent is expressed on the instrument of transfer. Wis. Stat. § 766.605.

Second, although title may not be an index to classification under the Act in other cases, a change in title may be relevant in a proceeding involving a classification issue. In some community property jurisdictions, for example, if a spouse with management and control rights changes title to an asset from his or her name to that of the other spouse, the change in title may indicate that the first spouse intended a gift of the asset to the other spouse as his or her separate property. *See Neely v. Neely*, 563 P.2d 302 (Ariz. Ct. App. 1977). On the other hand, in Wisconsin, it can be argued that shifting title proves nothing because it may simply be a device to transfer management and control from one spouse to the other.

How, then, may the basic presumption that all assets of spouses are classified as marital property be rebutted? The presumption is rebutted by proving that property is classified as other than marital property. Such proof will focus primarily on the time, method, or source of acquisition. The same factors are relevant if the presumption favorable to marital property classification is rebutted and an attempt is made to rebut the presumption favorable to deferred marital property. Note that when the presumption favorable to marital property classification is rebutted, the second presumption favorable to deferred marital property might still prevail. This could occur, for example, if the only proof available revealed an acquisition while the spouses were married but before the determination date. Sections 2.30–.33, *infra*, focus on proof required to rebut the presumption favorable to marital property classification. That discussion assumes that the spouses do not have a marital property agreement.

### 3. Time of Acquisition [§ 2.30]

The basic presumption favoring marital property classification may be rebutted by demonstrating that the time the asset was acquired (e.g., before marriage or after dissolution) establishes the asset's classification as predetermination date or individual property.

The time of acquisition may also be relevant in determining whether predetermination date property is subject to a deferred marital property election. A predetermination date asset acquired by a spouse while married—even an asset that clearly would have been classified as marital property had the Act applied when it was acquired—is not subject to disposition by the other spouse if the other spouse dies first after the determination date.

➤ **Example.** Assume that while married but before the determination date, a wife acquires and fully pays for real estate with her salary and that her husband predeceases her in 1990. The real estate clearly would have been classified as marital property upon the date of acquisition had the Act applied. Nonetheless, the deferred marital property election does not apply, *see infra* § 2.226, and the husband has no right to dispose of one-half of the real estate by his will. Proof that the date of acquisition was before the determination date may be needed to support that conclusion, however.

### 4. Method of Acquisition [§ 2.31]

The basic presumption in favor of marital property classification may be rebutted by demonstrating that a spouse acquired an asset either by gift or inheritance. Wis. Stat. § 766.31(7). Such assets are either individual property or predetermination date property and are not subject to the deferred marital property election. Other methods of acquiring individual or predetermination date property include court decrees so classifying the property, *see infra* § 2.119; certain payments in connection with a personal injury, *see infra* §§ 2.127–.134; unilateral statements, *see infra* §§ 2.70–.82; written consents (in the case of life insurance policies and assets used to pay premiums for such policies), *see infra* § 2.177; marital property agreements, *see infra* § 2.119; and certain recoveries under section 766.70, *see infra* § 2.120.

## 5. Source of Acquisition [§ 2.32]

The basic presumption favoring marital property classification may be rebutted by demonstrating that the source of payment for an acquisition was nonmarital property—a basic tracing concept.

➤ *Example.* If a wife demonstrates that during her marriage and after the determination date she sold an individual property asset and used the proceeds to purchase another asset in her name, that asset is successfully “traced” to the prior individual property and is classified as her individual property. *See* Wis. Stat. § 766.31(7)(b). On the other hand, if the wife had mixed the proceeds from the sale of the individual property asset in a bank account with her wages, and payments were made from the account and marital property funds deposited into it, the subsequent purchase of an asset in her name from that account might be classified as marital property because she might not be able to trace the acquisition to individual property. *See* Wis. Stat. § 766.63(1); *see infra* § 3.23.

## 6. Third Parties [§ 2.33]

Third parties may wish to rebut the presumption favorable to marital property classification. The IRS may attempt to rebut the presumption for tax purposes because a marital property asset receives an adjustment in basis in its entirety for income tax purposes at the death of a spouse regardless of the order of the spouses’ deaths. I.R.C. § 1014(a), (b)(6). The beneficiaries of the deceased spouse’s estate, however, may continue to treat the asset as former marital property. Indeed, if a court decree, such as a decree of a probate court, requires it, the beneficiaries might have to continue to so treat the asset. One commentator states that the strength of the presumption favorable to community property may reasonably vary with the length of the marriage, *see* McClanahan, *supra* § 2.4, at 335; thus, the strength of the presumption favorable to marital property in Wisconsin may similarly vary with the length of time elapsed after the determination date.

➤ *Example.* Assume that an untitled spouse with a Wisconsin domicile died on January 2, 1986, and that the surviving spouse was also then domiciled in Wisconsin. Assume that the spouses did not enter into a marital property agreement reclassifying their property as



marital property. (If an agreement had been entered into and death occurred within one year, the discussion in section 9.32, *infra*, would apply.) Should the property of the surviving titled spouse receive an adjustment in basis because of the presumption favorable to marital property classification? It is unlikely that in the absence of marital property agreements or gifts there will be much marital property owned by spouses with Wisconsin domiciles who die shortly after January 1, 1986, or another determination date. Thus, in most of these cases, there should be few assets classified as marital property that would be subject to the full adjustment in basis, because the presumption in favor of marital property classification can be easily rebutted.

## **E. Judicially Created Presumptions [§ 2.34]**

### **1. In General [§ 2.35]**

The presumptions regarding marital property classification and deferred marital property, *see supra* § 2.26, are the only presumptions the Act establishes for classification of property. Nevertheless, courts may fashion other presumptions to assist them in the classification process. *See infra* §§ 2.36–.37.

### **2. Proper Fund for Expenses [§ 2.36]**

A judicial presumption in some community property states is that expenditures for obligations that benefit the family and are made from a mixture of community and separate assets are made first from community assets. *See McClanahan, supra* § 2.4, at 341; *see also infra* § 3.20. A companion presumption is that an expenditure for a separate obligation is made from separate assets. *See McClanahan, supra* § 2.4, at 341. Generally used in tracing contexts, these two presumptions are based on the principle that the proper fund should be used to discharge obligations. *Id.*

### **3. Gift Presumptions [§ 2.37]**

Some community property states have developed presumptions in connection with interspousal gifts. *See infra* §§ 2.285–.288.

## V. Kinds of Marital Property [§ 2.38]

### A. Income Earned or Accrued During Marriage and After Determination Date [§ 2.39]

#### 1. In General [§ 2.40]

Section 766.31(4) provides that “[e]xcept as provided under subs. (7)(a), (7p) and (10), income earned or accrued by a spouse or attributable to property of a spouse during marriage and after the determination date is marital property.” Thus, as a general matter, marital property includes (1) income from personal services of a spouse earned or accrued during marriage and after the determination date and (2) income attributable to a spouse’s property earned or accrued during marriage and after the determination date. The three exceptions noted in section 766.31(4) are:

1. Income distributed to a spouse from a trust created by a third party, *see* Wis. Stat. § 766.31(7)(a); *see also infra* § 2.84;
2. Income attributable to nonmarital property subject to a unilateral statement under section 766.59, *see* Wis. Stat. § 766.31(7p); *see also infra* §§ 2.70–.82; and
3. Income attributable to property given by one spouse to the other unless it can be proven that the donor spouse had a contrary intent, *see* Wis. Stat. § 766.31(10); *see also infra* §§ 2.285–.288.

Other than these three exceptions and the exceptions for marital property agreements and court decrees providing otherwise, income earned or accrued by a spouse from *all* sources during marriage and after the determination date is marital property. Thus, income attributable to individual or predetermination date property, if earned or accrued by a spouse during marriage and after the determination date and if not subject to an exception, is marital property.

➤ **Note.** On this point, Wisconsin aligns itself with three other community property states—Idaho, Louisiana, and Texas—and the territory of Puerto Rico, which all follow the “civil law” rule on income. In the five other community property states—Arizona, California, Nevada, New Mexico, and Washington—income on

separate property remains separate, pursuant to the so-called American rule.

Understanding the scope of section 766.31(4) requires, first, a definition of the word *income*, *see infra* §§ 2.41–.55; second, an exploration of the concept of “income earned or accrued by a spouse or attributable to property of a spouse during marriage and after the determination date,” *see infra* §§ 2.56–.61; and third, a consideration of the various sources of income, *see infra* §§ 2.62–.89.

## **2. Definition [§ 2.41]**

Section 766.01(10) defines *income* as follows:

“Income” means wages, salaries, commissions, bonuses, gratuities, payments in kind, deferred employment benefits, proceeds, other than death benefits, of any health, accident or disability insurance policy or of any plan, fund, program or other arrangement providing benefits similar to those forms of insurance, other economic benefits having value attributable to the effort of a spouse, dividends, dividends on life insurance and annuity contracts to the extent that the aggregate of the dividends exceeds the aggregate premiums paid, interest, income distributed from trusts and estates, and net rents and other net returns attributable to investment, rental, licensing or other use of property, unless attributable to a return of capital or to appreciation.

## **3. What Definition Includes [§ 2.42]**

The definition of income is intentionally broad and is intended to include all forms of income and earnings. *See* UMPA § 1(10) cmt. The definition takes on more form, however, when one considers what it does not include. *See infra* §§ 2.43–.55.

## 4. What Definition Excludes [§ 2.43]

### a. Return of Capital [§ 2.44]

#### (1) In General [§ 2.45]

The definition of income expressly excludes a return of capital. Wis. Stat. § 766.01(10); UMPA § 1(10) cmt. The phrase “unless attributable to a return of capital” at the end of section 766.01(10) modifies all parts of the definition of income preceding it. UMPA § 1(10) cmt.; *see* Wis. Stat. Ann. § 766.01(10) Legis. Council Notes—1985 Act 37, §§ 69 to 73 (West 2009).

➤ **Example.** Assume that a husband invests \$200,000 of his individual property in a parcel of real estate that he holds for investment. The asset does not change in value, and he sells it during his marriage for \$200,000. Since he received only a return of his original capital, none of the return is income. Therefore, in the absence of tracing problems, a gift, or a marital property agreement or court decree to the contrary, none of the return is marital property.

The return-of-capital concept seems straightforward, but complex issues may arise for certain assets, as explained in sections 2.46–.48, *infra*.

#### (2) Wasting Assets [§ 2.46]

The Act does not deal specifically with the classification of wasting assets or proceeds received from such assets. A *wasting asset* is “[a]n asset exhausted through use or the loss of value, such as an oil well or a coal deposit.” *Black’s Law Dictionary* 135 (9th ed. 2009). Generally, the issue involved is whether as the asset is developed the proceeds received are considered to be either income or a return of capital. Consider, for example, a mineral deposit owned by a spouse as individual property. If proceeds received by the spouse as the mineral interest is developed are considered income, then eventually the entire asset is reclassified as marital property because unless one of the exceptions set forth in section 2.69, *infra*, applies, income earned or accrued by a spouse after the determination date is marital property.

Wis. Stat. § 766.31(4). If, on the other hand, the mineral proceeds are considered a return of capital, the proceeds are individual property.

As noted in section 3.27, *infra*, the issue is further complicated if the spouses use marital property funds to develop the asset or if a spouse performs substantial labor in connection with the development. Issues of mixing may then arise. The alternatives are either to allocate “all or nothing” to the individual interest based on the preponderance of value contributed or make an equitable apportionment between the individual and the marital property interests. The all-or-nothing rule provides certainty but may produce arbitrary results. The equitable apportionment approach (really a question of mixing) is difficult because the portions are not known when received, and thus subsequent mixing of funds is unavoidable.

The all-or-nothing approach was used in *Norris v. Vaughan*, 260 S.W.2d 676 (Tex. 1953). In that case, a husband owned undivided interests in various gas wells before marriage as his separate property. Pursuant to contracts entered into before the marriage, the wells produced gas during the marriage. Noting that the husband’s interest as lessee would last only so long as the gas was produced, the court held that the production and sale of the natural gas were equivalent to a piecemeal sale of the separate corpus, and that funds acquired through a sale of the separate corpus, if traced, would remain the husband’s separate property. The court applied the same rule to royalties paid for production of gas from separate property. The court distinguished the case from cases in which separate property was transformed into a new and more valuable state, such as by making clay into bricks or finished lumber from sawed timber. *See White v. Hugh Lynch & Co.*, 26 Tex. 195 (1862); *Craxton, Wood & Co. v. Ryan*, 3 Willson 439 (Tex. Ct. App. 1888). In these cases, said the *Norris* court, a great deal of community effort was required to effect the transformation. *Norris*, 260 S.W.2d at 680. It was, presumably, the effort involved rather than the fact that the property was transformed into a different state that required a different result.

For further discussion, see section 3.27, *infra*, Reppy & Samuel, *supra* § 2.19, at 155, and McClanahan, *supra* § 2.4, at 345.

### **(3) Stock Dividends [§ 2.47]**

Income as defined in section 766.01(10) includes dividends but excludes stock dividends and stock splits involving additional shares of the same company, since they simply spread the same value over more shares. *See* Reppy & Samuel, *supra* § 2.19, at 155–56; *accord* Ludwig v. Geise (*In re Geise*), 132 B.R. 908 (Bankr. E.D. Wis. 1991).

### **(4) Dividends on Life Insurance Policies and Annuities [§ 2.48]**

The definition of income in section 766.01(10) includes “dividends on life insurance and annuity contracts to the extent that the aggregate of the dividends exceeds the aggregate premiums paid.” This language is similar to that of I.R.C. § 72(e)(1)(B) and Treasury Regulation § 1.72-11(b)(1), which state that dividends used to reduce premiums are considered a return of premium and a reduction in the cost basis of the insurance contract, but that when aggregate dividends exceed the gross premiums paid, the excess is income. For more detail on this concept, see section 2.183, *infra*.

## **b. Appreciation [§ 2.49]**

### **(1) In General [§ 2.50]**

Income as defined by the Act does not include appreciation. *See* UMPA § 1(10) cmt. The phrase “unless attributable to ... appreciation” at the end of section 766.01(10) modifies all parts of the definition of income preceding it. *See* Wis. Stat. Ann. § 766.01(10) Legis. Council Notes—1985 Act 37, §§ 69 to 73 (West 2009); UMPA § 1(10) cmt. Section 766.01(2) defines the term *appreciation* as a “realized or unrealized increase in the value of property.”

➤ **Example.** Assume a spouse purchased real estate after the determination date with inherited cash for \$100,000 and a year later sold it for \$200,000. None of the proceeds is income. Whether the appreciation element is classified as marital property, however, depends on the nature of the appreciation. *See infra* §§ 2.90–.95, 3.27.

## (2) Business Entities [§ 2.51]

Classification questions may arise when one spouse owns a controlling interest in a business entity such as a corporation or partnership as his or her nonmarital property and may withdraw the income from the entity but instead permits the income to be used for the purchase of inventory or other assets or simply allows it to accumulate. If the income is withdrawn by the spouse during the marriage and after the determination date, it is marital property. Wis. Stat. § 766.31(4).

If a partnership, as opposed to a corporation, is involved, there may be an issue whether retained income maintains its status as income (or reclassifies a portion of the underlying partnership interest). For a discussion of this point, see section 3.45, *infra*. See also *Swope v. Swope*, 739 P.2d 273 (Idaho 1987) (superseded by statute, see *Marmon v. Marmon*, 825 P.2d 1136 (Idaho Ct. App. 1992)), in which the court, applying Idaho law, held that earnings of a separate property partnership, whether retained or distributed, are community property. The *Swope* court distinguished retained earnings of a corporation, holding that they do not constitute income and therefore community property unless they are distributed. A partnership, said the court, simply consists of the total of the interests owned by the partners and is directly controlled by the partners, whereas a corporation is a separate legal entity and is controlled only on a limited and indirect basis by the stockholders. The court also observed that under Idaho law a partner may direct payment of earnings and, if other partners disagree, dissolve the partnership and obtain the earnings. Stockholders have no equivalent rights.

➤ **Comment.** Whether the reasoning in *Swope* is persuasive in Wisconsin will depend, in part, on the nature of the partnership interest involved and on a comparison of Idaho and Wisconsin partnership law. A limited partnership interest, for example, is quite different from the interest described in *Swope* because, in the absence of an agreement to the contrary, a limited partner does not have the unilateral right to direct earnings, withdraw from a partnership, or dissolve a partnership. See Wis. Stat. ch. 179. The rights described in *Swope* appear to be those of a general partner. In Wisconsin, in the absence of an agreement to the contrary, the rights of general partners are described in chapters 178 and 179.

Income retained by a corporation is property of the corporation and is not marital property of the spouse. *See infra* § 3.45. However, the retained income may result in appreciation in the value of the shares of stock. The appreciation might or might not be marital property under rules set forth in section 766.63(2). Absent labor mixing that meets the tests of section 766.63(2), and absent fraud, it appears that no portion of the individual property corporate stock, including that attributable to retained income, is marital property. *See infra* § 3.45

It must be noted that there are no cases under the Act dealing with classification of appreciation of nonmarital property stock that is attributable to earnings retained by a corporation, and that the above analysis under the Act differs from that found in several dissolution cases when applying section 767.61. The differences are highlighted below. Section 767.61 provides that inherited property and property directly acquired with inherited property are not subject to property division in the absence of hardship. Section 767.61 has no counterpart under the Act. Rather, the Act has its own provisions dealing with appreciation; thus, the precedential value of these dissolution cases in the context of the Act must be approached with caution. Results on this issue may differ, therefore, depending on whether a marriage ends by dissolution or by death.

Two dissolution cases, *Lendman v. Lendman*, 157 Wis. 2d 606, 460 N.W.2d 781 (Ct. App. 1990), and *Metz v. Keener*, 215 Wis. 2d 626, 573 N.W.2d 865 (Ct. App. 1997), dealt with retained income in corporations, the stock of which was inherited property in the hands of a spouse. In *Lendman*, the income, stipulated to be a result of the husband-shareholder's labor, was used to retire debt. *Metz* involved an S corporation. Retained earnings were used to purchase new businesses. In addition, the wife-shareholder paid income tax on the retained earnings by reason of the pass-through nature of an S corporation.

Both decisions, relying on *Arneson v. Arneson*, 120 Wis. 2d 236, 244, 355 N.W.2d 16 (Ct. App. 1984), emphasized that income generated by an inherited asset is distinct from the asset itself. Thus, appreciation attributable to such income is not "directly acquired" by inheritance under section 767.61. Appreciation that results from market conditions, on the other hand, is inherently part of the asset and is directly acquired by inheritance. The court in *Lendman* noted that the income was a result of the husband's labor. The court in *Metz*, however, made no mention of



spousal labor and referred instead to the wife's full access, control, and right to the undistributed income.

Both courts agreed that retained earnings are not necessarily available to provide maintenance because they may be needed by the corporation for business purposes. Retained earnings are part of the marital estate for property division purposes, however. This is true, said the court in *Metz*, even though the wife-shareholder received compensation for her services to the corporation. The court relied on *Schorer v. Schorer*, 177 Wis. 2d 387, 407, 501 N.W.2d 916 (Ct. App. 1993), which said that the proposition that appreciation of a separate asset remains separate if the owning spouse has been compensated fairly for his or her efforts has not been given legal status in Wisconsin.

➤ **Comment.** The outcome may well be different under the Act. Generally, income retained by a corporation is not a marital property asset until it is distributed. See *infra* § 3.45. Section 766.01(10) defines income under the Act as items actually paid such as dividends, interest, wages, or net return resulting from use of property, but not return of capital or appreciation. The only type of appreciation of individual property (including inherited property) specifically mentioned in the Act that can be marital property is appreciation that the proponent can prove is substantial and was caused by substantial labor of either spouse that was not reasonably compensated. Wis. Stat. § 766.63(2). Thus, the conclusion described above in *Schorer* cannot be reached under the Act because reasonable compensation precludes the creation of marital property in connection with a spouse's application of efforts to nonmarital property. Appreciation resulting from causes other than labor of a spouse is likewise outside the ambit of section 766.63(2).

There is also authority, see, e.g., *Humphrey v. Humphrey*, 593 S.W.2d 824 (Tex. Civ. App. 1980); Reppy & Samuel, *supra* § 2.19, at 56, for the proposition that a spouse may not set up and use a corporate entity to defraud the other spouse.

### (3) Livestock [§ 2.52]

Issues involving livestock and farm animals have significance in Wisconsin. Are the proceeds received from the sale of livestock income,

appreciation, or (to some extent) return of capital? A review of a Wisconsin dissolution case and several cases from Texas may be helpful.

In *Preuss v. Preuss*, 195 Wis.2d 95, 536 N.W.2d 101 (Ct. App. 1995), a Wisconsin case involving a dissolution, the wife brought to the marriage 17 head of cattle she had inherited. She claimed that the offspring of these cattle should be treated as inherited property as well and excluded from the marital estate. The court disagreed, saying that animal offspring are “akin to dividends paid on gifted stock which are treated as income and are included in the marital estate.” *Id.* at 102.

➤ **Comment.** The *Preuss* decision has interesting economic consequences, and analogies to other types of assets can be imagined. Cattle will eventually die. Thus, the offspring might be thought of as a return of capital and therefore individual property. Otherwise, over time the individual property is inevitably converted into marital property without recompense to the owner of the individual property. See *supra* § 2.46, *infra* § 3.27 (discussing wasting assets). On the other hand, cattle can produce more offspring than needed to replace themselves. In this sense, the cattle and the offspring might be treated like marital property inventory, particularly if the spouse is in the business of buying and selling cattle. See *Moss v. Gibbs*, 370 S.W.2d 452 (Tex. 1963). Nevertheless, a court might hold that a reserve equal to the value of the inherited cattle should be set aside as individual property of the initial owner.

One early Texas case, *Stringfellow v. Sorrells*, 18 S.W. 689 (Tex. 1891), concerned a situation in which community labor was devoted to raising and fattening several mules separately owned by one spouse. The mules were subsequently sold. The court treated the sale proceeds as the owner spouse’s separate property. The court was unwilling to speculate about whether the appreciation in the mules’ value was a result of the owner spouse’s efforts or natural causes.

*Stringfellow* should be compared to a more recent Texas case, *Moss v. Gibbs*, 370 S.W.2d 452 (Tex. 1963). *Moss* concerned a wife who inherited cattle and several horses, then sold them, bought more, sold them, and so on. The court held that the wife was in the business of raising and selling livestock and that the sale proceeds were therefore income and community property. *Accord Ripatti v. Ripatti*, 494 P.2d 1025 (Idaho 1972).

➤ **Query.** What about proceeds from the sale of milk from dairy cows, wool from sheep, and the like? These proceeds will probably be considered income because they are regularly recurring items, somewhat like interest paid on a bond. A Texas case, *United States Fidelity & Guaranty Co. v. Milk Producers Ass'n*, 383 S.W.2d 181 (Tex. Civ. App. 1964), held that revenue from the sale of milk from a dairy herd is community property income even if the dairy cows are a spouse's separate property. On the question of whether the separate interest should be compensated, see the discussion in section 2.53, *infra*.

The holdings in the more recent Texas cases are also consistent with section 766.01(10), which provides that economic benefit having value attributable to a spouse's effort is included in the definition of income.

#### **(4) Farming Operations [§ 2.53]**

Generally, farm income attributable to spousal efforts during marriage is community property even if the land or farming machinery involved is one spouse's separate property. *See, e.g., Riggers v. Riggers*, 347 P.2d 762 (Idaho 1959); *Cleveland v. Cole*, 65 Tex. 402 (1886). California follows the American rule that income from separate property is separate. *See supra* § 2.40. Nonetheless, in that state, income produced by a farming operation owned as separate property and attributable to one spouse's efforts is community property. *See Mayhood v. La Rosa*, 374 P.2d 805 (Cal. 1962). Under this approach, no recompense is given to the owner for the use of the owner's separate property, land, or machinery even though that land and machinery may depreciate in value as the result of such use.

Whether Wisconsin will adopt an apportionment approach (in effect providing some return for the owner of the individual property) is a matter for speculation. If a spouse executes a unilateral statement in connection with nonmarital property land or machinery, the apportionment issue may arise—namely, how much of the income is subject to the unilateral statement because it is attributable to the nonmarital capital assets employed, and how much is attributable to spousal effort (and is therefore classified as marital property)? *See infra* § 2.76.

### c. Certain Death Benefits and Policies [§ 2.54]

Income as defined by the Act does not include death benefits under any health, accident, or disability insurance policy or under any plan, fund, or other arrangement providing benefits similar to those forms of insurance. Wis. Stat. § 766.01(10).

Thus, under section 766.01(10), health, accident, and disability insurance proceeds, other than death benefits, are income. Consequently, the proceeds from disability policies (other than death benefits) are income whether the proceeds are paid from disability policies constituting a benefit of employment or from policies purchased by a spouse as other than a benefit of employment. As to classification of such benefits, see sections 2.136 and 2.196–.199, *infra*.

### d. Certain Expenses [§ 2.55]

Income as defined by the Act includes “net rents and other net returns attributable to investment, rental, licensing or other use of property.” Wis. Stat. § 766.01(10). Thus, income earned but used to pay expenses attributable to investment, rental, licensing, or other use of property is not included in the definition of income.

This rule is similar to the net-income rule in Idaho. In *Martsch v. Martsch*, 645 P.2d 882 (Idaho 1982), the court permitted payment of property taxes on separate property from rents earned by that property. The court reasoned that a contrary rule would require those amounts to be reimbursed to the community and would ultimately dissipate the separate property.

➤ **Comment.** The terms *net rents* and *net returns* in section 766.01(10) presumably take into account a reasonable allowance for depreciation and replacement (e.g., by the use of straight-line depreciation over the reasonable life of an asset), although the matter is not clear. This interpretation would permit a reserve from income for recurring replacements of such major items as roofs and furnaces, which are subject to wear and tear but are not covered by annual expenditures for ordinary repairs. If such a reserve is permitted, it is unclear whether a segregated reserve account must actually be

established. At the least, creation of such an account minimizes mixing and tracing problems.

## **B. Meaning of Earned or Accrued [§ 2.56]**

### **1. In General [§ 2.57]**

Income is marital property only if it is “earned or accrued ... during marriage and after the determination date.” Wis. Stat. § 766.31(4). Section 766.01(8) defines the term during marriage to include periods when both spouses are domiciled in Wisconsin and to exclude periods when either or both of the spouses are not domiciled in Wisconsin. It follows that income earned or accrued before or after the period defined by the Act as during marriage is not marital property.

Although the Act does not define *earned or accrued*, it is clear that a purpose behind the phrase is to solve certain “front-end” and “tail-end” problems. Regarding the front-end problem, the comment to section 4 of UMPA states that the difficulty “pertains to income received shortly after the determination date from effort or accrual of rights before the determination date. Actual ownership of such property became fixed before the determination date and it should not be and is not classified as marital property.” (Emphasis added.)

The potential tail-end problem pertains to disintegrating marriages (although a change of domicile by either or both spouses to or from another state poses a similar problem). Here, the concern is that a cash-basis or actual-receipt rule might permit a former spouse (or a spouse changing domicile) to delay receipt of income under his or her management and control until after dissolution (or the change of domicile), thereby prejudicing the former spouse. The “accrual or constructive receipt system” is used to solve that problem. UMPA § 4 cmt. (Equitable division principles applicable at a dissolution, *see infra* ch. 11, also have considerable importance, but those principles are not referred to in the comment to section 4 of UMPA.)

## 2. Work Performed on Same Job Before and After Determination Date [§ 2.58]

Under section 766.31(4), income is marital property if “earned or accrued by a spouse ... during marriage and after the determination date.” As noted in section 2.57, *supra*, this rule leaves a front-end problem relating to income earned by a spouse on the same job both before and after the determination date. Is such income marital property, nonmarital property, or both? At issue is whether the words “earned or accrued” apportion income or mean that income does not accrue until the right to receive it is fixed as a matter of contract law.

➤ **Comment.** It is a precondition that the item must actually be income as opposed to a gift. In one case, *Holby v. Holby*, 638 P.2d 1359 (Ariz. Ct. App. 1981), the wife’s employer gave her shares of Procter & Gamble stock for several years. Each year, the wife was given a choice of receiving either cash or the stock, and she chose the stock. The trial court found the stock to be gifts and therefore the wife’s separate property. The appellate court reversed, saying that even though it was received at Christmas and labeled a gift, the stock was, in fact, a bonus for services rendered.

➤ **Example.** Assume that a married artist will receive a commission after completing and delivering a painting; half the painting is completed before the determination date, but the painting is finished during marriage and delivered after the determination date. On the one hand, because the right to the commission became “fixed” during marriage and after the determination date, the entire commission might be treated as marital property and none of it apportioned in accordance with the time when labor was expended. On the other hand, a court might find that half the commission was earned before the determination date and should be treated as the artist’s nonmarital property.

Support for apportionment may be found in two cases involving attorney fees owed to an attorney spouse, *Waters v. Waters*, 170 P.2d 494 (Cal. Ct. App. 1946), and *Due v. Due*, 342 So. 2d 161 (La. 1977). In each case, the court awarded the nonattorney spouse an interest in contingent fees earned by but not yet paid to the attorney spouse by the date of the divorce. The apportionment approach not only seems more equitable but should also resolve the companion issue involving

allocation of expenses incurred. In the example, the artist spent money for paint, canvas, and the like before the determination date. However, if the test is when income becomes fixed, those expenses may not be matched against the income ultimately received, unless the artist is entitled to reimbursement for them from marital property.

Under an apportionment approach, the commission for the painting may be a mixed asset. However, if the services rendered before the determination date cannot be adequately traced (perhaps because accurate work records were not kept), the asset may be deemed entirely marital property under section 766.63.

### **3. Work Performed on Same Job During Marriage and After Termination of Period Defined as During Marriage [§ 2.59]**

A problem similar to that discussed in section 2.58, *supra*, arises, for example, with an artist who paints half a picture during marriage and after the determination date, is then divorced, and completes and delivers the painting after the dissolution of the marriage. Because of the Act's definition of the term during marriage, a similar problem also arises if before completion of the painting either (1) the artist or his or her spouse changes domicile to another state or (2) the artist's spouse dies. The artist's commission is not fixed at dissolution, and there may be no property interest to divide. On the other hand, a divorce court has substantial equitable powers and might assign a value to the contract and divide it at dissolution, much as divorce courts do with unvested pension plans.

Such a division occurred in *Skaden v. Skaden*, 566 P.2d 249 (Cal. 1977). In that case, an insurance agent executed an agreement during the course of his marriage that conditioned his right to receive renewal commissions after his termination from service on his refraining from competitive activities. In the divorce judgment, the court equated his right to the commissions to vested but unmatured pension benefits. The court then assigned a value to the commissions and divided them.

#### **4. All Work Performed Either Before or During Marriage; Income Received Either During Marriage or After Period Defined as During Marriage [§ 2.60]**

➤ *Example.* Assume that a woman writes a book and enters into a royalty agreement with her publisher while she is single, then marries and subsequently receives royalties during marriage. Are any of the royalties received during marriage marital property? It would appear the answer is no, even though the royalties probably constitute income under section 766.01(10), because the contractual rights and performance that yielded the income were established before the marriage. Compare this result with *In re Marriage of Gillespie*, 948 P.2d 1338 (Wash. Ct. App. 1997), which involved payments received by a spouse during marriage with respect to a covenant not to compete, which was signed by the spouse before marriage in connection with stock that the spouse acquired before the marriage but sold during the marriage. The court held those payments were the spouse's separate property, although it explicitly noted that the spouse's earnings through new employment after marriage actually increased, leaving the question whether the court would have reached a different result if the spouse's earnings had decreased.

See also the discussion of *In re Marriage of Gillespie* at section 2.277, *infra*.

An issue involving work performed during marriage but royalties received after marriage arose in *Worth v. Worth*, 241 Cal. Rptr. 135 (Ct. App. 1987), which involved a dissolution proceeding in California. While an author was married, he wrote two books, copyrighted them, and entered into an agreement with his publisher. The court first rejected an argument based on federal preemption that a protected work is the author's separate property. (Accord *Rodrique v. Rodrique*, 218 F.3d 432 (5th Cir. 2000), on the issue of preemption.) The court went on to hold that because all the effort was performed during the marriage, all benefits flowing from that effort (including damages that might be received as a result of a copyright-infringement action commenced during the marriage) were community property subject to division at dissolution.



## 5. Awards Made After Period Defined as During Marriage [§ 2.61]

Questions can arise as to the classification of awards made after the termination of the period defined as during marriage. These questions may focus on the purpose of the award, i.e., is it designed to compensate for past services during marriage, or is the right to an award created after marriage simply the result of an employer's beneficence?

Many of these questions are considered in *Frahm v. Frahm*, 53 Cal. Rptr. 2d 31 (Ct. App. 1996), which involved a severance package received by the husband after the dissolution of the parties' marriage. The wife contended that a portion of the severance should be awarded to her as community property. The severance payments were made as an incentive to employees voluntarily to separate themselves from the employer. The court found that the right to the benefits resulted from the employer's beneficence and accrued after the marriage was dissolved; therefore, the severance payment was the husband's separate property.

The decision includes a good summary of cases in this area and concludes as follows:

[T]he results are inconsistent. For example, the *Horn* court [*Horn v. Horn*, 226 Cal. Rptr. 666 (Ct. App. 1986)], found the payment's contractual basis rather than its purpose determinative of its character; in *Bane* [*Bane v. State*, 256 Cal. Rptr. 468 (Ct. App. 1989)], the court discounted the absence of a contract and focused instead on the benefit's purpose, and in *Lawson* [*Lawson v. Lawson*, 256 Cal. Rptr. 283 (Ct. App. 1989)], the court ignored the tie between the benefit and length of employment, because the right to the benefit resulted from conditions beyond the husband's control and accrued after the marriage ended.

53 Cal. Rptr. 2d at 36.

## C. Sources of Income Classified as Marital Property [§ 2.62]

### 1. In General [§ 2.63]

The general rule at section 766.31(4) is that income earned or accrued by a spouse during marriage and after the determination date is classified as marital property. The principal exceptions include:

1. Income classified as other than marital property by a marital property agreement, *see infra* § 2.284, or by court decree, Wis. Stat. § 766.31(10); *see infra* §§ 2.105, .119;
2. Distributions to a spouse from a trust created by a third person (unless the trust provides otherwise), Wis. Stat. § 766.31(7)(a); *see infra* § 2.84;
3. Income attributable to nonmarital property subject to an effective unilateral statement under section 766.59, Wis. Stat. § 766.31(7p); *see infra* §§ 2.70–.82; and
4. Income generated by property given by one spouse to the other unless a contrary intent of the donor spouse can be established regarding such income, *see* Wis. Stat. § 766.31(10); *see also infra* §§ 2.86–.88.

Thus, the general rule is that all income earned or accrued by a spouse during marriage and after the determination date is marital property, whether the income is attributable to (1) a spouse's efforts during marriage and after the determination date or (2) a spouse's property. These two broad categories contain within them the many sources of marital property income discussed in sections 2.64–.89, *infra*.

### 2. Compensation [§ 2.64]

The most common source of income is the compensation and other remuneration a spouse earns or accrues during marriage and after the determination date for his or her services rendered after the determination date. This includes compensation in all its various forms: salary, wages, tips, stock options, commissions, bonuses, partnership

compensation, and payments in kind for services. Wis. Stat. § 766.01(10).

➤ **Note.** A unilateral statement does not apply to compensation income. *See infra* §§ 2.70–82.

Certain benefits of employment such as club memberships and use of automobiles may be considered compensation. If such benefits are not compensation, they constitute income if they have value because they constitute economic benefits having value attributable to a spouse's effort. *See* Wis. Stat. § 766.01(10); *see also infra* § 2.66. Consequently, such benefits are income and therefore marital property if they have monetary value and are earned or accrued by a spouse during marriage and after the determination date.

### **3. Deferred-employment-benefit Plans [§ 2.65]**

The definition of income in section 766.01(10) specifically refers to deferred-employment-benefit proceeds. Since compensation earned or accrued by a spouse during marriage and after the determination date is clearly marital property, so are benefits under deferred-employment-benefit plans based on the time of employment giving rise to the benefit during marriage and after the determination date. Wis. Stat. § 766.62.

Deferred-employment-benefit plans are given unique treatment under the Act in a number of respects that are covered in sections 2.184–219, *infra*. Two characteristics are noted here, however. First, under sections 766.31(3) and 766.62(5), the nonemployee spouse's marital property interest in a deferred-employment-benefit plan terminates at that spouse's death if he or she predeceases the employee spouse. *See infra* § 2.201. Second, section 766.62 provides special rules for classifying deferred employment benefits. *See infra* §§ 2.186–199.

Regarding the applicability of a unilateral statement to deferred-employment-benefit plans, see sections 2.70–82, *infra*.

### **4. Economic Benefit Attributable to Effort [§ 2.66]**

Section 766.01(10) includes in the definition of income “economic benefits having value attributable to the effort of a spouse.” How

broadly this definition will be interpreted is unclear. It would seem to include proceeds received from management of a rental property or from activities in connection with a sole proprietorship, an unincorporated farm, and the like. See the discussion of livestock and farming operations, for example, at sections 2.52 and 2.53, *supra*. Regarding income accumulated inside an entity, see section 3.29, *infra*, and for the impact of a unilateral statement, see sections 2.70–.82, *infra*.

If not considered compensation, certain benefits of employment (club memberships, use of automobiles, etc.) constitute income if they have value, because they are economic benefits having value attributable to a spouse's effort. See *supra* § 2.64. Consequently, if the benefits have value they are marital property to the extent earned or accrued by a spouse during marriage and after the determination date. Wis. Stat. § 766.31(4).

## **5. Income Attributable to Certain Business Enterprises [§ 2.67]**

Income earned or accrued by a spouse during marriage and after the determination date and attributable to a sole proprietorship is marital property whether or not the spouse's efforts are involved. Section 766.31(4) is broadly worded and (unless one of the exceptions in section 2.69, *infra*, applies) classifies as marital property the income earned or accrued by a spouse during marriage and after the determination date from any source, without reference to whether the income is attributable to a spouse's efforts. Whether income results from efforts or from the underlying investment may be relevant if a spouse owns a sole proprietorship as nonmarital property and executes an effective unilateral statement. Questions of apportionment of the income may then arise. See *infra* §§ 2.70–.82. Generally, income distributed by partnerships and dividends paid on corporate stock to a spouse during marriage and after the determination date are marital property. Regarding income retained by an entity, see section 2.51, *supra*, and section 3.46, *infra*; for the impact of a unilateral statement, see sections 2.70–.82, *infra*; and for the rule in connection with interspousal gifts, see section 766.31(10).

## 6. Income Attributable to Marital Property [§ 2.68]

The income earned or accrued by a spouse during marriage and after the determination date attributable to assets classified as marital property is likewise classified as marital property. Wis. Stat. § 766.31(4); UMPA § 4 cmt.

## 7. Income Attributable to Individual and Predetermination Date Property [§ 2.69]

Generally, income earned or accrued during marriage and after the determination date and attributable to assets classified as a spouse's individual property is marital property. *See* UMPA prefatory note; Wis. Stat. § 766.31(4); *see supra* § 2.8 (statutory definition of during marriage). Exceptions include:

1. Income from individual property received as a gift from the other spouse, unless a contrary intent with respect to the income can be established, *see* Wis. Stat. § 766.31(10); *see infra* §§ 2.86–.88.
2. Income from individual property subject to a unilateral statement, Wis. Stat. § 766.31(7p); *see infra* §§ 2.70–.82;
3. Income from individual property subject to a marital property agreement or court decree classifying income as other than marital property, Wis. Stat. § 766.31(7)(d); and
4. Income and principal distributed to a spouse after the determination date from a trust created by a third party, unless the trust provides otherwise, Wis. Stat. § 766.31(7)(a); *see infra* § 2.84.

➤ **Example 1.** Assume that a wife inherits stock from her father during marriage and after the determination date. The stock is her individual property. However, the cash dividends (other than as a return of capital) she receives that are attributable to the stock during marriage and after the determination date are classified as marital property unless one of the above exceptions applies.

The same analysis applies to income attributable to predetermination date property. Thus, subject to the same exceptions for income from

individual property, income earned or accrued during marriage and after the determination date attributable to a spouse's predetermination date property is marital property. Wis. Stat. § 766.31(4); UMPA § 2 cmt.

➤ **Example 2.** If the wife in Example 1 acquired stock by inheritance or gift from a person other than her husband while married and before the determination date, that stock is predetermination date property. However, the cash dividends (other than a return of capital) she receives on the stock during marriage and after the determination date are marital property unless one of the above exceptions applies.

## **8. Exception for Income Attributable to Nonmarital Property and Subject to Unilateral Statement**

### **[§ 2.70]**

#### **a. In General [§ 2.71]**

In Wisconsin, a spouse may classify income attributable to his or her nonmarital property as individual property if the spouse properly implements a unilateral statement to that effect. The unilateral statement concept is not part of UMPA but is based on the so-called Louisiana fruits rule, *see* La. Civ. Code Ann. art. 2339 (West, WESTLAW current through the 2009 regular session).

The full statutory scheme involving the unilateral statement consists of provisions of sections 766.31(4), 766.31(7p), 766.31(10), and 766.59. Section 766.31(4) states the basic rule that income earned or accrued by a spouse or attributable to property of a spouse during marriage and after the determination date is marital property. *See supra* § 2.8 (statutory definition of during marriage). The section's introductory clause creates exceptions to the rule, however, including two described in subsections 766.31(7p) and (10). Section 766.31(7p) states that income attributable to all or specified property other than marital property with respect to which a spouse has executed a unilateral statement is individual property. Section 766.31(10) states, in part, that spouses may reclassify their property not only by gift or marital property agreement but also by a unilateral statement under section 766.59. Section 766.59 is the operative section in this statutory scheme. Subsection (1) states the general rule governing the execution of unilateral statements; subsections

(2) to (4) give the basic administrative and mechanical aspects of the statement; and subsection (5) describes the impact a unilateral statement has on third parties.

Section 766.59(1) states: “A spouse may unilaterally execute a written statement which classifies the income attributable to all or certain of that spouse’s property other than marital property as individual property.” Clearly, the statement may be executed unilaterally and without the other spouse’s consent or participation.

➤ **Example.** Assume that a wife inherits IBM stock from her mother during marriage and after the determination date. That stock is her individual property, but the dividends attributable to that stock during marriage and after the determination date are marital property unless she executes a unilateral statement (or unless another of the exceptions described in section 2.69, *supra*, applies). If she executes a unilateral statement, the dividends accruing after the statement’s effective date are her individual property. The unilateral statement is not executed unless signed by the wife and acknowledged by a notary. *See* Wis. Stat. § 766.59(2)(a). If the wife executed the unilateral statement before January 1, 1986, it was effective on January 1, 1986, or at such later time as provided in the statement. If she executed the unilateral statement on or after January 1, 1986, it was effective when executed or at such later time as provided in the statement. *Id.*

A unilateral statement may be executed before marriage. Wis. Stat. § 766.59(6). Within five days after a unilateral statement is signed, the “executing spouse” (or person intending to be married) must notify the person whom the executing spouse intends to marry or has married by either personally delivering a copy to the person the executing spouse intends to marry (or has married) or sending a copy by certified mail to the address of the person the “executing spouse” intends to marry (or has married). Wis. Stat. § 766.59(2)(b), (6). Failure to give notice apparently does not render the unilateral statement ineffective; rather, it gives rise to a breach of the duty of good faith imposed by section 766.15. *See* Wis. Stat. § 766.59(2)(b), (6). The unilateral statement is effective when executed, not when the other spouse receives notice of the statement. Wis. Stat. § 766.59(2)(a). A unilateral statement (and its revocation) may be recorded in the county register of deeds office under section 59.43(1)(r), Wis. Stat. § 766.59(2)(c), (4), and in connection with real estate under chapter 706.

**b. Scope of Unilateral Statement [§ 2.72]****(1) Applicable Only to Income Attributable to Other Than Marital Property [§ 2.73]**

A unilateral statement may apply only to income attributable to assets classified as other than marital property. Wis. Stat. § 766.59(1). A unilateral statement may not apply to income attributable to assets classified as marital property. If nonmarital and marital property assets are mixed but the various components can be identified, a unilateral statement applies only to the income that accrues after the statement's effective date and that is attributable to the nonmarital portion. A unilateral statement applies to income attributable to nonmarital property assets of all types; thus, it applies to income attributable to individual property and to income attributable to predetermination date property, even income that may be deferred marital property subject to the deferred marital property election by a surviving spouse.

**(2) Income Attributable to Designated and After-acquired Nonmarital Property [§ 2.74]**

Section 766.59(3) refers to income from "property designated in the statement," and section 766.31(7p) refers to a unilateral statement that may apply to all or specified property other than marital property. The language in these two sections should permit the terms of a unilateral statement to apply to the income that accrues after the statement's effective date and that is attributable to assets other than marital property owned at the statement's effective date. It is also apparent that a unilateral statement may designate certain items of nonmarital property, rather than all items of nonmarital property, the income of which is classified as individual property.

Unilateral statements are superfluous in at least three situations:

1. A unilateral statement is not necessary in connection with an interspousal gift. If the gift is intended to be the donee spouse's individual property, the income is also the donee spouse's individual



property unless a contrary intent of the donor is established. Wis. Stat. § 766.31(10); *see infra* §§ 2.86–.88, .285–.288.

2. A unilateral statement is not necessary to classify distributions of income (and principal) to a spouse from a trust created by a third party as that spouse's individual property. Wis. Stat. § 766.31(7)(a); *see infra* § 2.84.
3. A unilateral statement is not necessary if a marital property agreement classifies income as individual property. Wis. Stat. § 766.17(1); *see infra* ch. 7.

### (3) Before or During Marriage and Prospective Only [§ 2.75]

All income that is attributable to the nonmarital property designated in the unilateral statement, and that accrues on or after the statement's effective date and before any revocation, is the individual property of the spouse who owns the property and executed the statement. Wis. Stat. § 766.59(3). A unilateral statement acts prospectively only; a unilateral statement may not apply to income that accrued on nonmarital property before the statement's effective date and may not reclassify such income, contrary to a possible implication of section 766.31(10), *see infra* § 2.289. Since it is prospective, a unilateral statement does not have any impact on income of predetermination date property that accrues while spouses are married and before the determination date; in short, the statement affects neither the characterization of such income as deferred marital property nor any mixing that occurred before the statement's effective date. *See* Wis. Stat. Ann. § 766.59 Legis. Council Committee Supplemental Notes Relating to 1985 Act 37 (West 2009). However, if income of predetermination date property that accrues while spouses are married and before the determination date is reinvested in nonmarital property, the income accruing from that reinvestment during marriage and after a statement's effective date is subject to the statement.

➤ **Note.** Section 766.59(3) uses the word “accrues.” There may be cases in which (1) income accrues before a statement is effective but is actually received after the effective date or (2) income accrues before a statement is revoked or terminated but is actually received

after the revocation or termination. *See supra* § 2.57 (analysis of similar problem).

A unilateral statement executed during the marriage applies only to income accruing during the marriage after the statement's effective date. Wis. Stat. § 766.59(3). Thus, a unilateral statement is not effective for a subsequent marriage; a new statement is needed. A person intending to marry may execute a unilateral statement as if married. Wis. Stat. § 766.59(6). The statement is effective upon the marriage or at a later time, if so provided in the statement.

#### **(4) Income Attributable to Efforts [§ 2.76]**

A unilateral statement may apply only to income attributable to nonmarital property. A unilateral statement may not apply to income attributable to services or efforts. *See* Wis. Stat. Ann. § 766.59 Legis. Council Committee Supplemental Notes Relating to 1985 Act 37 (West 2009). If either spouse expends effort on nonmarital property that is subject to a unilateral statement, a question of apportionment arises. How much of the income is attributable to nonmarital property subject to the unilateral statement, and how much is marital property because it is an economic benefit having value attributable to a spouse's effort during marriage and after the determination date? *See* Wis. Stat. §§ 766.01(10), .31(4); *see also supra* § 2.8 (statutory definition of during marriage). Assume, for example, that a spouse devotes effort to managing a rental property that is his or her individual property and that he or she executes a unilateral statement. How much of the rent is subject to the statement and how much is marital property? As the Nevada Supreme Court put it in *Cord v. Neuhoff*, 573 P.2d 1170, 1173 (Nev. 1978), "It is evident that these concepts come into conflict when a spouse devotes his time, labor, and skill to the production of income from separate property."

➤ **Comment.** Nevada employs the American rule that income on separate property remains separate, *see supra* § 2.40. Therefore, in Nevada a unilateral statement is irrelevant. Nevertheless, when unilateral statements and spousal efforts come together in Wisconsin, cases from American-rule jurisdictions may be useful. The court in *Cord* explained that in each American-rule jurisdiction there must be apportionment of any increment in value between the owner's separate estate (individual property) and the community (marital property) and that all jurisdictions require an apportionment between

the separate estate and the community. *Cord*, 573 P.2d at 1173. However, the result in *Cord* must be compared with the all-or-nothing approach described in sections 2.46 and 2.53, *supra*. For further discussion of the mixing problem, see section 3.48, *infra*.

#### **(5) Income Attributable to Invested Compensation and Deferred-employment-benefit Plans [§ 2.77]**

A unilateral statement may not apply to a spouse's compensation for services rendered after the determination date because a unilateral statement applies only to income attributable to nonmarital property. What about income resulting from compensation that was earned before the determination date and is traceably invested in stock, real estate, and the like? A unilateral statement could apply to income from the investment accruing after the statement's effective date. Similarly, a unilateral statement may extend to earnings inside deferred-employment-benefit plans attributable to predetermination date employment. However, the impact of a statement on such earnings is minimized in any event because of section 766.62, which in effect apportions earnings in a plan, as well as contributions, pursuant to a formula based on time of employment before and after the determination date. *See infra* § 2.197. Moreover, the definition of income in section 766.01(10) does not apply to trust income until it is distributed. Wis. Stat. Ann. § 766.01(10) Legis. Council Notes—1985 Act 37, §§ 69 to 73 (West 2009). Thus, for plans involving trusts, it is not clear whether a unilateral statement applies to the income while it is accumulated. *But see infra* § 2.78.

#### **(6) Income Inside Entities [§ 2.78]**

Generally, income inside entities is not income for purposes of the Act and therefore is not subject to a unilateral statement. Income retained by a corporation, for example, may result in appreciation of the interest in the entity (such as the stock), but it is not income as defined under the Act. Generally, income exists only when it is distributed to a shareholder. As to these points and for treatment of partnerships, see section 2.51, *supra*, and section 3.29, *infra*.

Income accumulated by a trust should be carefully examined, however. Section 766.01(10) provides that until it is distributed, income generated by a trust or estate is not income for purposes of the Act. Wis. Stat. Ann. § 766.01(10) Legis. Council Notes—1985 Act 37, §§ 69 to 73 (West 2009). The impact of this rule may differ depending on the type of trust at issue.

In the case of a trust created by a third party for a spouse's benefit, the rule's impact is academic because income distributed to the spouse from the trust after the determination date is the spouse's individual property even if a unilateral statement is not executed. Wis. Stat. § 766.31(7)(a); *see infra* § 2.84.

In the case of a revocable trust created by a spouse and funded with that spouse's nonmarital property, a literal reading of section 766.01(10) would suggest that a unilateral statement will not apply to income accumulated by the trust after the statement's effective date. *See also* Wis. Stat. Ann. § 766.01(10) Legis. Council Notes—1985 Act 37, §§ 69 to 73 (West 2009). However, a strong argument can be made that the existence of the revocable trust should be ignored. The settlor spouse with management and control rights merely changed the form of ownership. Although management and control of the asset now shift to the trustee, the settlor may regain full management and control on demand. A revocable trust differs from a trust created for a spouse's benefit by a third person, in which the beneficial interests in the trust are determined by the third person and are gifts by the third person to a spouse. Thus, income accumulating after the determination date in a revocable trust created by a spouse should be treated as income (i.e., as "earned or accrued") under section 766.01(10) and should be susceptible to classification as individual property by a unilateral statement to the extent the income accrues after the statement's effective date.

### **(7) Income Attributable to Joint-tenancy or Tenancy-in-common Property [§ 2.79]**

A joint tenancy or tenancy in common created before the determination date between spouses only or between a spouse or spouses and a third party may exist at the determination date, or such a tenancy may be created by a spouse or spouses with a third party after the determination date. *See* Wis. Stat. § 766.60(4)(a). There appears to be no reason why a unilateral statement could not apply to a spouse's

interest in the income accruing after the statement's effective date and attributable to nonmarital property in the tenancy. *See infra* § 2.83.

### **c. Revocation of Unilateral Statement [§ 2.80]**

Section 766.59(4) provides that a unilateral statement may be revoked in writing by the executing spouse. After revocation, the Act's general classification rules apply to income attributable to the property and accruing after the revocation. It appears (although it is not expressly stated) that a revocation does not retroactively reclassify income that accrued while the statement was in effect. A revoking spouse must notify the other spouse of the revocation by personally delivering a copy to the other spouse or by sending a copy by certified mail to the other spouse's last-known address. The revocation may be recorded in the county register of deeds office under section 59.43(1)(r). Wis. Stat. § 766.59(4).

The formalities needed to revoke a unilateral statement should be compared with the formalities needed to make the execution of a unilateral statement effective. Both a statement and a revocation must be in writing. However, the requirements for notice to the other spouse differ for a statement and a revocation. A spouse (or person intending to marry) executing a unilateral statement must notify the other spouse (or the person he or she intends to marry) of the statement's contents within five days after the statement is signed by personally delivering a copy to the other spouse (or the person he or she intends to marry) or by sending a copy by certified mail to that other person's last-known address. A failure to give the notice is a breach of the duty of good faith. Wis. Stat. § 766.59(2)(b), (6). In contrast, section 766.59(4) specifies no time limit for delivery of a notice of revocation to the other spouse (or the person intended to be married), nor does it state that a failure to give a notice of revocation is a breach of the duty of good faith. It is arguable that a revocation is a declaration against interest and that therefore no delivery should be required. Nonetheless, it appears that delivery of a revocation may be a requirement to make the revocation effective. On the other hand, the effectiveness of the execution of the statement itself does not depend on delivery. *See supra* § 2.71.

#### **d. Effect of Unilateral Statement on Third Parties [§ 2.81]**

With respect to its effect on third parties, a unilateral statement or its revocation is treated as if it were a marital property agreement. Wis. Stat. § 766.59(5). For example, unless a creditor has actual knowledge of a unilateral statement or its revocation before the spouses incur an obligation or enter into an open-end plan, the unilateral statement or its revocation cannot adversely affect the creditor's interest. Wis. Stat. §§ 766.55(4m), .56(2)(c). The recording of a unilateral statement or its revocation under section 59.43(1)(r) does not constitute notice to third parties. Wis. Stat. § 766.56(2)(a). A unilateral statement or its revocation, like a marital property agreement, may be recorded in the chain of title under chapter 706 and constitutes notice to third parties in connection with the real estate involved. *See id.*

#### **e. Planning Considerations [§ 2.82]**

A unilateral statement may be used to increase assets classified as individual property. A statement may also be used to avoid or minimize certain mixing problems, especially when no income from spousal efforts is involved. Income earned or accrued by a spouse during marriage and after the determination date from nonmarital property is marital property if the spouse does not have a unilateral statement or some other applicable exception noted in section 2.69, *supra*; if, for example, such income is reinvested along with nonmarital property or used to reduce principal on mortgages on nonmarital property, mixing or reimbursement problems will occur. Wis. Stat. § 766.63(1). Although these problems may be avoided or minimized by using a unilateral statement, a mixing problem may nevertheless result if a spouse's efforts are applied to the underlying property subject to the statement. Wis. Stat. § 766.63(2); *see also supra* § 2.76, *infra* § 3.48. Furthermore, if the individual income is later mixed with assets classified as marital property and cannot be traced, it is reclassified. Wis. Stat. § 766.63(1). If the individual income is mixed with property that is deferred marital property and cannot be traced, it is subject to the deferred marital property election. Wis. Stat. §§ 766.63(1), 861.02(2)(a); *see also, infra* ch. 10. Finally, it should be noted that a unilateral statement does not remove the income involved from the assets otherwise available for division in a dissolution proceeding.

## **9. Income Attributable to Joint-tenancy Property and Tenancy-in-common Property [§ 2.83]**

If the spouses do not have a marital property agreement, a document of title, instrument of transfer, or bill of sale used in an attempt to create a joint tenancy or tenancy in common exclusively between spouses after the determination date results in survivorship marital property or marital property, respectively. Wis. Stat. § 766.60(4)(b)1.a., b. If withdrawn, the income earned or accrued by a spouse during marriage and after the determination date and attributable to such an asset is marital property. Wis. Stat. § 766.31(4). Income attributable to the asset and not withdrawn is presumably survivorship marital property or marital property, respectively. Wis. Stat. § 766.60(4)(b)1.a., b.; *see infra* §§ 2.257, .258.

If a third party gives property in joint tenancy or tenancy in common to both spouses after the determination date, the property is survivorship marital property or marital property, respectively, unless the donor provides otherwise. Wis. Stat. § 766.60(4)(b)2. Assuming that the donor does not provide otherwise, the treatment of income withdrawn or not withdrawn should be the same as that described in the immediately preceding paragraph in connection with survivorship marital property or marital property, respectively.

If, however, after the determination date, the donor provides for a traditional joint tenancy or tenancy in common for both spouses, the income earned and withdrawn is marital property in the absence of a unilateral statement, interspousal gift, or marital property agreement or court decree to the contrary. *See* Wis. Stat. § 766.31(4). Reinvested income has the incidents of traditional joint-tenancy or tenancy-in-common property, as the case may be. *See* Wis. Stat. § 766.60(4)(b)2.

A joint tenancy or tenancy in common may have been either created exclusively between spouses before the determination date or given by a third party to spouses exclusively before the determination date. The traditional incidents of ownership of such tenancies control to the extent they conflict with incidents of property classification under chapter 766. Wis. Stat. § 766.60(4)(a). Income earned and withdrawn from such tenancies after the determination date is marital property unless one of the exceptions noted in section 2.69, *supra*, applies. Wis. Stat. § 766.31(4). Income that is not withdrawn, however, will probably be

given traditional joint-tenancy or tenancy-in-common treatment, as appropriate. *See infra* § 2.255.

A joint tenancy or tenancy in common may have been created between a spouse or spouses and a third party before the determination date. Such tenancies are recognized with all their traditional incidents of ownership to the extent they conflict with incidents of property classification under chapter 766. Wis. Stat. § 766.60(4)(a). Income earned and withdrawn by a spouse from such a tenancy after the determination date is marital property under section 766.31(4), unless one of the exceptions noted in section 2.69, *supra*, applies.

With regard to unwithdrawn income earned during marriage and before the determination date in connection with a joint tenancy created by a spouse and a third party, the decedent's fractional share is potentially part of the augmented marital property estate subject to election. *See* Wis. Stat. §§ 861.02, .03(2). Whether unwithdrawn income earned after the determination date is treated as a gift from the tenant spouse to the third party subject to the nontenant spouse's right of reimbursement under section 766.70(6)(c) is considered in section 8.57, *infra*.

A joint tenancy or tenancy in common may be created between a spouse and a third party after the determination date. If the spouse uses marital property cash to fund the arrangement, the cash is a gift to the third party subject to the nontenant spouse's right of reimbursement under section 766.70(6)(c). Whether the right of reimbursement extends to unwithdrawn income attributable to the property is considered in section 8.57, *infra*. Income withdrawn by a spouse is marital property under section 766.31(4) unless one of the exceptions noted in section 2.69, *supra*, applies. What if nonmarital property is used to fund the tenancy? Whether unwithdrawn income earned after the determination date is subject to the nontenant spouse's right of reimbursement under section 766.70(6)(c) is considered in section 8.57, *infra*.

## **10. Exception for Distributions to Spouse from Trust Created by Third Party [§ 2.84]**

An important exception to the income rule of section 766.31(4) concerns postdetermination date distributions to a spouse from a trust created by a third party. A distribution of income from a trust is included



in the definition of income in section 766.01(10). However, section 766.31(7)(a) provides that income distributed during marriage and after the determination date from a trust created by a third person is the individual property of the spouse to whom it is distributed unless the trust provides otherwise. Section 766.31(7)(a) has no counterpart in UMPA.

Thus, in the absence of a marital property agreement or court decree to the contrary, an interspousal gift, or a unilateral statement, income generated by assets received by a spouse as an outright gift from a third person is treated quite differently from income received by that same spouse from a trust created by the same third-party donor. In the first case, the income is marital property; in the second, it is individual property, unless the trust provides otherwise. Consequently, a donor who does not wish a donee's spouse to have a marital property interest in the income of donated assets should consider using a trust.

If a trust is created by the third party for the benefit of both spouses, a distribution made to only one spouse should be treated as that spouse's individual property (unless the trust provides otherwise or one of the other exceptions noted in the preceding paragraph applies) because (1) the language of section 766.31(7)(a) focuses on whether a distribution is made to one spouse as opposed to both spouses and (2) it is consistent with the policy behind the provision to treat such a distribution as a gift at the time of distribution. A postdetermination date distribution to both spouses as joint tenants or as tenants in common is presumably survivorship marital property or marital property of the spouses unless the trust provides otherwise. Wis. Stat. § 766.60(4)(b)2.

Section 766.31(7)(a) does not apply to income distributed from a trust created by a spouse for the benefit of that spouse or the other spouse. *See infra* §§ 2.98–.104. As to income accumulated inside a revocable trust created by a spouse, see section 2.78, *supra*, and sections 2.101, .103, *infra*.

## **11. Net Probate Income [§ 2.85]**

How will the net probate income accumulating during marriage and after the determination date in an estate of a third party, the beneficiary of which is a spouse, be classified? Net probate income remaining in an estate is not within the definition of income in section 766.01(10).

However, when the net probate income is distributed from the estate, it becomes income for purposes of section 766.01(10). *See* Wis. Stat. Ann. § 766.01(10) Legis. Council Notes—1985 Act 37, §§ 69 to 73 (West 2009). Therefore, in the absence of an effective unilateral statement or other applicable exception noted in section 2.69, *supra*, the income is marital property. (By contrast, income distributed to a spouse from a trust created by a third party is individual property unless the trust provides otherwise. Wis. Stat. § 766.31(7)(a); *see supra* § 2.84.) It may be advantageous to issue a separate check representing the net probate income to the beneficiary entitled to the income. *See infra* § 12.177.

In the absence of an effective unilateral statement or other applicable exception noted in section 2.69, *supra*, the income attributable to a specific bequest or devise and distributed to a spouse after the determination date should be marital property because it is income earned or accrued by the spouse during marriage and after the determination date on a gift from a third party. *See* Wis. Stat. § 766.31(7)(a). If the beneficiary of an estate is a trust, all net probate income flowing from the estate to the trust and from the trust to a trust beneficiary pursuant to section 701.20 should be individual property (unless the trust provides otherwise) because it is trust income distributed to a spouse during marriage and after the determination date from a trust created by a third party. *See id.*

## **12. Exception for Income on Interspousal Gifts**

### **[§ 2.86]**

#### **a. After Determination Date [§ 2.87]**

A completed gift of property from one spouse to the other after the determination date that is intended to be the donee's individual property reclassifies the property as the donee's individual property. Wis. Stat. § 766.31(10). It may be necessary to show donative intent so that no other interpretation can be attached to the transfer. It is probably safest to show donative intent with a signed writing. Is the income from the property also classified as the donee's individual property? Section 766.31(10) answers that question in the affirmative by stating that if a spouse gives property to the other spouse and intends when the gift is made that the property be the donee's individual property, the income from the property is also the donee's individual property unless a

contrary intent of the donor regarding the classification of income is established. The burden of proving that the income is not individual property should be on the donor or persons claiming through the donor. *Cf.* Tex. Const. art. XVI, § 15 (creating presumption that income from property given by one spouse to other spouse is donee's separate property); *see also* La. Civ. Code Ann. art. 2343 (West, WESTLAW current through the 2009 regular session) (providing that income from community asset donated by one spouse to other spouse is donee's separate property unless otherwise provided in act of donation). For planning aspects, *see* chapter 10, *infra*.

### **b. Before Determination Date [§ 2.88]**

Assume that before the determination date, one spouse gave income-producing property to the other spouse while the two were married and intended the property to be the donee spouse's solely owned property. How would predetermination date and postdetermination date income from that gift be treated? The question reveals a gap in the Act—namely, the lack of any specific provision dealing with interspousal gifts of predetermination date property made before the determination date.

Section 766.31(4) specifically states that, subject to certain exceptions, all income from property earned or accrued by a spouse during marriage and after the determination date is marital property. *See supra* § 2.8 (statutory definition of during marriage). Moreover, the Act's general scheme is that all property of spouses is marital property unless classified otherwise. Wis. Stat. § 766.31(1). Section 766.31(10) refers only to gifts that are intended to be the donee spouse's *individual* property, *see supra* § 2.87, and predetermination date property by definition is not individual property, *see* UMPA § 4 cmt.

Arguably, the policy of section 766.31(10) should be extended to the income from interspousal gifts of predetermination date property made before the determination date. Pursuant to that policy, income earned or accrued by a spouse before the determination date attributable to an interspousal gift completed before the determination date would be treated as the donee spouse's solely owned property (solely owned because technically it cannot be individual property) unless it could be established that the donor spouse intended otherwise. Assuming that the income was intended to be the donee spouse's solely owned property, such income would not be deferred marital property subject to election of

the surviving spouse under section 861.02 because if the Act had been in effect when the gift was made, the income from the gift would have been the donee spouse's individual property. Similarly, income from such a gift earned or accrued by the donee spouse during marriage and after the determination date would be that spouse's individual property.

The result in *Poindexter v. Poindexter*, 142 Wis. 2d 517, 419 N.W.2d 223 (1988), is inconsistent with the immediately preceding analysis. In *Poindexter*, the Wisconsin Supreme Court considered whether income from a gift of rental property made by a husband to his second wife before the determination date was to be considered by the court in setting maintenance payments to the husband's former spouse; the classification issues are relevant here. The court held that the rental property acquired by the second wife was predetermination date property because the gift was made to her before January 1, 1986, the couple's determination date. Noting that under section 766.31(9), property acquired before the determination date is treated "as if it were individual property" and that income from a spouse's individual property accruing during marriage and after the determination date is marital property, the court held that the rental income was marital property and that the husband owned a one-half interest. *Id.* at 539–40. The decision makes no reference to section 766.31(10), which states that when property is given by one spouse to the other and the donor spouse intends that the property be the donee spouse's individual property, the income from the gift is the donee spouse's individual property unless the donor spouse indicates an intent to the contrary. Thus, the court did not discuss why the classification rules for the income from predetermination date property acquired by interspousal gift should differ from the rules applicable to income from postdetermination date property acquired by interspousal gift.

### **13. Income Substitutes and Personal-injury Awards**

#### **[§ 2.89]**

A spouse's income may be lost as a result of injury or disability. The characterization of personal-injury awards and income substitutes is considered in sections 2.127–.139, *infra*.

## **D. Appreciation [§ 2.90]**

### **1. In General [§ 2.91]**

The drafters of the Act made major decisions concerning classification of the appreciation of marital, individual, and predetermination date property. Sections 2.92–.95, *infra*, deal with appreciation other than an increase in value as a result of additional investment.

### **2. Appreciation of Marital Property [§ 2.92]**

All appreciation of a marital property asset is marital property because no other classification is provided for it. UMPA § 4 cmt.; Wis. Stat. § 766.31(1).

### **3. Appreciation of Individual Property [§ 2.93]**

Appreciation of individual property may have to be apportioned between individual and marital property classifications. Under section 766.63(2), substantial appreciation of individual property that results from the substantial undercompensated labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity of either spouse is marital property. All other appreciation of individual property (such as that resulting from market conditions or that failing to meet the tests set forth in section 766.63(2), even if spousal efforts are involved) is individual property. Wis. Stat. §§ 766.31(7)(c), .63(2); *see also infra* ch. 3 (particularly sections 3.44–.48).

The court cited section 766.63(2) and applied similar reasoning in *Haldemann v. Haldemann*, 145 Wis. 2d 296, 426 N.W.2d 107 (Ct. App. 1988), a dissolution proceeding. The court held that appreciation (without indication that it must be substantial) of a spouse's nondivisible property that resulted from the other spouse's uncompensated effort beyond that normally required by the marital relationship was divisible at dissolution. *See infra* § 11.16.

*Kobylski v. Hellstern (In re Estate of Kobylski)*, 178 Wis. 2d 158, 503 N.W.2d 369 (Ct. App. 1993), involved a wife's personal residence that

was classified as individual property. Improvements to the residence were paid for from marital property funds. The husband performed labor on the residence, thereby allegedly increasing its value. The court distinguished improvements and appreciation attributable to cash payments from improvements and appreciation resulting from the husband's labor. As to whether the cash payments created a marital property interest in the home or simply a right of reimbursement, the court held that the improvements take the classification of the underlying property (in this case, individual property) and that the "marital estate" has a right of reimbursement equal to the enhanced value attributable to the improvements (as opposed to a right of reimbursement under a dollar-for-dollar-expenditure reimbursement theory). Expenditures that relate merely to the maintenance of property or that do not enhance the property's value are not to be considered. *Id.* at 176–80. On the other hand, labor mixing that meets the tests under section 766.63(2) creates an ownership interest measured by the appreciation attributable to that labor. *Id.* at 185; *see infra* § 3.42.

Issues involving spousal efforts resulting in appreciation of individual property closely held stock are considered in section 2.51, *supra*.

#### **4. Appreciation of Predetermination Date Property [§ 2.94]**

Appreciation of predetermination date property is considered at sections 2.149–.153, *infra*.

#### **5. Appreciation of Mixed Property [§ 2.95]**

If an asset has individual and marital property components and the individual property component can be traced, the asset is mixed property. Wis. Stat. § 766.63(1); *see infra* ch. 3. As to whether the appreciation of such an asset is apportioned between the individual and marital property components or whether there is simply a claim for reimbursement, see sections 3.11 and .42, *infra*.

### **E. Property Reclassified Through Mixing When Tracing Is Impossible [§ 2.96]**

Section 766.63(1), an extremely important statutory provision, states that except as provided in connection with life insurance policies and deferred-employment-benefit plans, mixing marital property with property having any other classification reclassifies the other property to marital property unless the nonmarital component of the mixed property can be traced. If, for example, marital property wages are deposited in an account containing inherited cash, and subsequent activity in the account causes mixing to the point that tracing the nonmarital component is impossible, the entire account balance becomes marital property. Similar mixing reclassification occurs when the proceeds from the sale of nonmarital property are mixed with marital property. *See infra* ch. 3. Treatment as deferred marital property may occur in some instances. *See infra* §§ 2.235–.237, .238, 3.4.

### **F. Third-party Gifts to Both Spouses [§ 2.97]**

A postdetermination date gift made during lifetime or at death by a third party to both spouses is marital property, survivorship marital property, joint-tenancy property, or tenancy-in-common property, depending on the donor's intent. Section 766.60(4)(b)2. provides that if, after the determination date, a third party gives property to both spouses titled in joint tenancy exclusively between the spouses, it is survivorship marital property unless the donor provides otherwise. If a third party gives property in the form of a tenancy in common exclusively between spouses after the determination date, the property is marital property unless the donor provides otherwise. Thus, under this statute, use of the words *joint tenancy* or *tenancy in common* without more is not sufficient to create a joint tenancy or tenancy in common. *See id.* Of course, a donor could give property to both spouses as marital property or as survivorship marital property.

➤ **Comment.** The inclusion of section 766.60(4)(b)2. in the Act establishes that a third-party donor's expression of the intent to create a joint tenancy or a tenancy in common exclusively between spouses after the determination date is recognized in Wisconsin, despite any implications to the contrary based on UMPA. Section 4 of UMPA, on which section 766.31(7)(a) is based, provides that a gift made

during lifetime or at death by a third person to only one spouse during marriage and after the determination date is individual property. A gift made to both spouses, on the other hand, is marital property, states the comment to UMPA section 4, and this rule applies to gifts to both spouses in any form, including transfers to the spouses as joint tenants or tenants in common. UMPA § 4 cmt. Clearly, the inclusion in the Marital Property Act of section 766.60(4)(b)2., for which there is no corresponding provision in UMPA, represents a change from UMPA and is intended to override the comment to UMPA section 4 and any implication based on that comment in section 766.31(7)(a).

The rule set forth in section 766.60(4)(b)2. is similar to the holding in *In re Marriage of Martin*, 645 P.2d 1148 (Wash. Ct. App. 1982). In *Martin*, the court approved a suggestion made by Professor Harry Cross in *The Community Property Law in Washington*, 49 Wash. L. Rev. 729, 750 (1974), that a gift to both spouses by a third party should be presumptively community property in the absence of proof of the donor's different intent.

As to gifts made to both spouses by a third party before the determination date, see section 2.255, *infra*.

## **G. Marital Property Transferred to Trust by Spouse or Spouses [§ 2.98]**

### **1. Living Trusts [§ 2.99]**

#### **a. In General [§ 2.100]**

Section 766.31(5) provides: “The transfer of property to a trust does not by itself change the classification of the property.” This language replaced language in the Act as originally enacted providing that “marital property transferred to a trust remains marital property.” Wis. Stat. Ann. § 766.31(5) Legis. Council Notes—1985 Act 37, §§ 76 to 83 (West 2009). The replacement was made because the latter provision “raised many questions.” *Id.* Under the revised language, the mere transfer of a marital property asset to a trust does not change the classification of the property transferred. *Id.*



## **b. Revocable Trusts [§ 2.101]**

The revised language of section 766.31(5), *see supra* § 2.100, applies to revocable trusts. Indeed, the comment to section 4 of UMPA, on which the originally enacted language was based, states that the “principal enabling function” of former section 766.31(5) was to permit the creation of revocable living trusts by one or both spouses without any automatic reclassification of the property committed to the trust. Revocable trusts holding marital property assets should avoid probate as to the transferor, *see* Steven L. Nelson, *The Community Property Agreement: A Probate Cure with Side Effects*, 11 Comm. Prop. J. 185 (1984), but may be reached by creditors under such provisions as sections 701.06(6) and 701.07(3).

➤ **Example.** Assume that a wife unilaterally creates a revocable trust and that she transfers to it a marital property asset over which she has management and control. The transfer does not by itself reclassify the asset, and a completed gift has not been made until the wife can no longer revoke the trust. Thus, depending on the terms of the revocable trust, the trust may hold assets classified as marital property.

If the revocable trust holds assets classified as marital property and the wife dies survived by her husband, the husband has a claim under section 766.70(6)(b)1. to recover his interest in the former marital property assets held by the trust or distributed to a third-party beneficiary. The spouses, by documentation, could change that result. *See infra* ch. 10. The assets are “former marital property” because marital property cannot exist after one spouse dies. *See* UMPA § 4 cmt. The wife’s share of the former-marital-property assets passes under the terms of the trust. There may be gift tax consequences for the husband if he does not claim his share of the former-marital-property assets at his wife’s death when the trust becomes irrevocable. *See infra* § 9.91.

If, on the other hand, the husband dies first, his will or the laws of intestacy dispose of his interest in the former-marital-property assets transferred to the trust; the wife’s interest in the former-marital-property assets remains in the trust. *See infra* §§ 10.36, .62; *see also infra* § 10.61 (sample form).

If both spouses act together in creating a revocable trust, the transfer of marital property assets to the trust does not by itself reclassify the property. However, the trust's terms could direct a reclassification. *See infra* ch. 10. It may also be possible that spouses acting together could inadvertently reclassify marital property assets by putting terms into a revocable trust that are inherently inconsistent with the nature of marital property. *See, e.g., infra* § 10.36.

### **c. Irrevocable Trusts [§ 2.102]**

Section 766.31(5) states that a transfer of property to a trust does not “by itself” change the classification of the property. If something is added to the transfer, the clear implication is that marital property interests in the property are reclassified (or divested) to the extent no interests are retained. (Transfers with retained interests and interests provided for the other spouse are discussed later in this section.) In the case of an irrevocable trust, the fact of the trust's irrevocability (a necessary element of a completed gift) should, by itself, supply the additional element needed to reclassify the property from the moment of transfer, even if one spouse unilaterally transfers a marital property asset to an irrevocable trust. Such a transfer should result in a completed gift and thus should be subject to remedies provided to the other spouse.

If the trust's irrevocability by itself does not suffice to reclassify the property (and neither section 766.31(5) nor the Legislative Council notes on the section specifically state that it does, *see* Wis. Stat. Ann. § 766.31(5) Legis. Council Notes—1985 Act 37, §§ 76 to 83 (West 2009)), the act of both spouses transferring a marital property asset to an irrevocable trust for a third person's benefit should provide the additional element needed to reclassify the property and to divest both spouses of any marital property interest in the property. If such a transfer is made directly to an individual, it is a completed gift; the result should be the same if a trust is involved. In short, in the situation posed, a completed gift is made.

But what if a spouse with management and control unilaterally transfers marital property to an irrevocable trust solely for a third party's benefit and the other spouse does not assert his or her rights to recover the gift property within the time prescribed by section 766.70(6)(a)? Does the property remain marital property, or is the transfer a completed gift when the time expires for the nonparticipating spouse to reclaim the

property transferred to the trust? It is fair to conclude that at the moment that a spouse unilaterally transfers marital property to an irrevocable trust for a third person's sole benefit, all marital property interests are reclassified and the transfer is a completed gift subject to the remedies provided to the other spouse, including those under section 766.70(6)(a), if the dollar amounts of section 766.53 are exceeded.

The result should be the same if a spouse with management and control creates and funds an irrevocable trust with a marital property asset and retains an income interest in the trust but provides a remainder interest for a third person. The transfer "by itself" does not reclassify the property. But the fact of irrevocability should divest and reclassify marital property interests, at least in the remainder interest, from the moment of transfer. This should be true even though the settlor spouse retained a valuable property right (the life-income interest) and the designation of a third person as remainder beneficiary denies the nonparticipating spouse the right to dispose of his or her interest in the remainder at death if remedies are not asserted under section 766.70(6)(a). For purposes of sections 766.53 and 766.70(6)(a), the retained interest is ignored in valuing the gift to the trust; the full value of the property is the value of the gift, and that value determines whether the nonparticipating spouse has a remedy under section 766.70(6)(a). Thus, from the nonparticipating spouse's point of view, the valuation of the gift and the maximum amount that may be recovered in connection with a transfer to a trust when the donor spouse retains an interest do not differ from the remedy provided in connection with an outright gift of the entire asset.

That the nonparticipating spouse loses the right to dispose of his or her marital property interest at death does not alter this conclusion. That is the consequence of a completed gift to an individual when the other spouse fails to assert available remedies within the time prescribed in section 766.70(6)(a), and the same rules should apply when irrevocable trusts are involved.

If the settlor spouse unilaterally creates a trust, funds it with assets classified as marital property, and provides an income interest for the other spouse with the remainder to a third person, a similar set of problems and answers may arise for the nonsettlor spouse. But there are some differences, too. For purposes of determining the relevant dollar values, section 766.53 refers to an interest donated to a spouse, but it does so only in the context of an income interest retained by the donor

spouse. Section 766.53 does not specifically deal with a case in which the donor spouse does not retain an interest but instead provides an income interest for the other spouse. The nonsettlor spouse's income interest may or may not be his or her individual property as a gift from the settlor spouse pursuant to section 766.31(10). The answer could turn on the trust's terms or the settlor's intent. If the nonsettlor spouse does not acquiesce in this arrangement, then for purposes of sections 766.53 and 766.70(6)(a) the income interest given the other spouse presumably should be ignored so that the full value of the property is the value for gift and recovery purposes.

➤ **Practice Tip.** The planner can eliminate any uncertainty about the classification of the property committed to an irrevocable trust by having both spouses act together in transferring the property to the trust. An alternative is to ensure that no asset classified as marital property is transferred to the trust. A marital property agreement, for example, could reclassify marital property assets as the settlor spouse's individual property assets before the transfer to the trust is made.

For analysis of the powers of trustees in connection with trusts holding assets classified as marital property, see section 4.61, *infra*.

#### **d. Accumulated Income [§ 2.103]**

Income may be accumulated by a revocable trust created by a spouse unilaterally and funded with marital property assets. The transfer to the trust is not a completed gift, and thus the property transferred should retain its character as marital property under section 766.31(5). The proper analysis is that the accumulated income is also marital property. This should be true despite the implication of section 766.01(10) that trust income is not income for purposes of the Act until distributed. *See* Wis. Stat. Ann. § 766.01(10) Legis. Council Notes—1985 Act 37, §§ 69 to 73 (West 2009). That implication is inappropriate for revocable trusts. Although there is no specific language in the Act supporting it, a strong argument can be made that income accumulated during marriage and after the determination date in a revocable trust created by a spouse should be included in the definition of income for purposes of the Act. The trust was created by a spouse with management and control over the assets, and simply changing the form of holding to a revocable trust should not alter the nature of the income accumulated or the spouses'

rights with respect to it. Thus, if a settlor spouse unilaterally commits marital property assets to a revocable trust and income is accumulated by the trust during marriage and after the determination date, and if the nonsettlor spouse dies first, sound policy dictates that the deceased spouse's estate has an interest in the income.

If a spouse creates a revocable trust and commits his or her nonmarital property assets to the trust, income accumulated during marriage and after the determination date is marital property; however, a unilateral statement executed by the settlor spouse should apply to the income accumulated by the trust after the statement's effective date. *See supra* § 2.78. If the income retained by the revocable trust is income for purposes of the Act (and there is no unilateral statement), section 766.63(1) appears to apply: that is, if nonmarital property assets committed to the trust cannot be traced because the income is reinvested in the trust, the assets fluctuate in value, and withdrawals are made from time to time, all the trust assets may, as a result of mixing, be reclassified as marital property.

Income may be accumulated in an irrevocable trust created unilaterally by a spouse for a third person's sole benefit. Even if assets classified as marital property are transferred to the trust, all marital property interests in the donated property should be reclassified because the transfer is a completed gift. However, the nonsettlor spouse has remedies including that under section 766.70(6)(a) if the dollar amounts of section 766.53 are exceeded. *See infra* § 8.45.

➤ **Example.** Assume a spouse establishes an irrevocable trust with marital property assets and retains a mandatory income interest, with the remainder made payable to a third person. Income distributed to the settlor spouse after the determination date is marital property under subsection 766.31(4) or (1). How is the income classified if it is allowed to accumulate? Assume that the time for invoking a remedy under section 766.70(6)(a) has passed.

Before considering the classification of the income interest in the above example, it should be noted that the remainder interest in the example is reclassified because it is a completed gift. The other spouse's failure to assert a remedy under section 766.70(6)(a) means that the assets committed to the trust may not be reclaimed as marital property.

Nevertheless, the failure to assert a remedy should not mean that the retained income interest is also reclassified. The retained interest is an interest in property under the broad definition of property in section 766.01(15), which includes equitable interests. That interest has not been transferred, and the accumulated income is the settlor's upon demand.

Consideration must also be given to section 766.01(10), which implies that income retained in a trust is not income for purposes of the Act. The analysis used in the preceding paragraphs for revocable trusts should apply. The trust was created by a spouse with management and control over the assets. Simply changing the form of holding the income to that of a trust over whose income the settlor retains full control should not alter classification of the income. The accumulated income should remain marital property. A gift of that income, therefore, is not complete until the settlor dies, at which time the right to demand the income expires and a remedy under section 766.70(6)(b) may be invoked by the nonsettlor spouse with respect to it.

If the above analysis is incorrect and the income interest is reclassified along with the remainder interest when the assets are transferred to the trust, then the nonsettlor spouse must assert his or her remedy under section 766.70(6)(a), which applies regardless of the interest retained by the settlor spouse.

➤ **Practice Tip.** Until the issue discussed above is fully resolved, a nonsettlor spouse may wish to assert the remedy under section 766.70(6)(a) within the time prescribed.

What if the irrevocable trust provides only a discretionary interest in income (not subject to ascertainable standards) for the settlor spouse? The income is marital property under subsection 766.31(4) or (1) if it is distributed to the spouse during marriage and after the determination date. What if the income is accumulated? A settlor spouse has no enforceable right to the income, the equitable interest in the income interest expires at the settlor's death, and there appears to be no transfer at that time. Of course, the nonsettlor spouse has remedies, including that under section 766.70(6)(a). It would appear that the time within which to assert such a remedy begins upon the transfer to the trust.

## 2. Testamentary Trusts [§ 2.104]

When a spouse dies leaving a will that creates a testamentary trust, the trust cannot be funded with marital property assets because marital property can be owned only by living spouses. UMPA § 4 cmt. Rather, the trust is funded with the decedent's share of former marital property and nonmarital property.

With respect to forced and unforced elections in connection with trusts, see chapter 10, *infra*.

### H. Marital Property Acquired by Decree [§ 2.105]

Section 766.31(7)(d) states that individual property may be acquired during marriage and after the determination date by court decree. *See supra* § 2.8 (statutory definition of during marriage). There is no similar language in section 766.31 referring to acquisition of marital property by decree, and none is needed because all property of spouses is marital property, except that which is classified otherwise by chapter 766. At dissolution, the parties own former marital property assets as equal tenants in common unless the decree or an agreement entered into by the former spouses after dissolution provides otherwise. Wis. Stat. § 766.75. Section 766.70(2) permits a court to order an accounting; determine rights of ownership in, beneficial enjoyment of, or access to marital property; and determine the classification of all property of the spouses. *See infra* §§ 8.20–22. On the other hand, if marital property assets have been or are likely to be substantially injured by a spouse's gross mismanagement, waste, or absence, section 766.70(4) permits a court to order a change in the classification of marital property. *See infra* § 8.31. A spouse's recovery during marriage and after the determination date for damage to property under section 766.70 is individual property, except as specifically provided otherwise in a decree or marital property agreement. Wis. Stat. § 766.31(7)(e); *see infra* § 8.38. After a spouse's death, a probate court may determine the classification of property. Wis. Stat. § 857.01. As to personal-injury awards, see sections 2.127–.134, *infra*.

Recoveries for damage to marital property are discussed in section 2.125, *infra*.

## VI. Individual Property [§ 2.106]

### A. Definition [§ 2.107]

Individual property is a creation of the Act. With one exception, it can be acquired only after the determination date by a spouse. The exception (not found in UMPA) involves property owned by a spouse at a marriage occurring after January 1, 1986, if both spouses have a Wisconsin domicile when they marry. Wis. Stat. § 766.31(6). Other than this exception, all property acquired before the determination date is not individual property and is referred to in this chapter as predetermination date property. Predetermination date property, by definition, is not a type of individual property. The comment to UMPA section 4 states: “Property in existence prior to adoption [of UMPA] is not individual property, by definition, since the classification of individual property is a creation of [UMPA]. Property in existence prior to adoption of [UMPA] is whatever it is without [UMPA].”

### B. Attributes [§ 2.108]

The comment to section 4 of UMPA explains that except for the income attributable to individual property earned or accrued by a spouse during marriage and after the determination date (which income is generally marital property), individual property is analogous to solely owned property in common law jurisdictions.

➤ **Note.** Individual property differs from solely owned property in common law jurisdictions in two important respects. Unlike solely owned property of a deceased spouse in a common law jurisdiction, individual property of a deceased spouse with a Wisconsin domicile is not subject to a surviving spouse’s elective rights. Further, although income attributable to individual property is generally classified as marital property, it may be classified as individual property if it is subject to one of the exceptions noted in section 2.69, *supra*.

During marriage, a spouse may manage and control his or her individual property and regulate its income, even though the income may be marital property, *see* Wis. Stat. §§ 766.51(1)(a), (am), .15(2). The owner of individual property may unilaterally make gifts of the property,



sell the property, pledge the property, and otherwise manage and control the property free of limitations (other than those described in sections 861.17 and 767.61, noted below, and in connection with a homestead, *see* Wis. Stat. § 706.02(1)(f)). For a full explanation of the rules of management and control, *see* chapter 3, *infra*.

At death, unless section 861.17(1) (pertaining to property transferred in fraud of a surviving spouse) applies, and subject to the right to allowances under chapter 861, the owner may dispose of his or her individual property without limitation. As noted above, individual property owned by a deceased spouse with a Wisconsin domicile is not subject to a surviving spouse's elective rights, unlike solely owned property in a common law jurisdiction.

Individual property retains that status at all times unless reclassified by mixing, marital property agreement, or other means of reclassification provided by the Act. *See infra* §§ 2.283–.295. Proof is necessary, however, to rebut the general presumption that all spouses' property is marital property, or at death, to rebut the secondary presumption that it is deferred marital property. *See* Wis. Stat. §§ 766.31(2), 861.02(2)(a).

Rights over individual property are not unlimited, however. A court in an equitable proceeding may subject individual property to a surviving spouse's rights if arrangements are made in fraud of that spouse's rights under chapter 852 (intestacy) and chapter 861 (allowances). Wis. Stat. § 861.17(1); *see infra* § 12.168 (discussing section 861.17(1) reference to intestacy and allowances). In addition, individual property is subject to property division under section 767.61 in dissolution proceedings.

## **VII. Kinds of Individual Property [§ 2.109]**

### **A. Property Owned at Marriage Taking Place After January 1, 1986 [§ 2.110]**

Section 766.31(6) states that “[p]roperty owned at a marriage which occurs after 12:01 a.m. on January 1, 1986, is individual property of the owning spouse if, at the marriage, both spouses are domiciled in this state.”

➤ **Example.** Assume that a marriage occurs on January 10, 1990, the wife owns property at the marriage, and both spouses are domiciled in Wisconsin at the time of marriage. Whether acquired before or after January 1, 1986, by purchase, gift, inheritance, or other means, the wife's property is her individual property. It retains that status during her marriage as long as it is not reclassified by mixing, marital property agreement, or other means provided by the Act. *See infra* part XIII.

The Act does not classify property owned by a spouse at a marriage that occurs after January 1, 1986, if either spouse, at marriage, has a marital domicile in another state but later both spouses establish a Wisconsin domicile. Such property is neither individual nor marital property. *See* Wis. Stat. Ann. § 766.31(6) Legis. Council Notes—1985 Act 37, §§ 76 to 83 (West 2009). In the absence of subsequent mixing, a marital property agreement, or other means of reclassification provided by the Act, such property must be predetermination date property that would have been individual property if the Act had then applied. Similarly, the Act does not classify property owned by a spouse at a marriage occurring before January 1, 1986, even if both spouses are domiciled in Wisconsin when they marry. Again, without subsequent mixing, a marital property agreement, or other means of reclassification under the Act, this property is a type of predetermination date property that would have been individual property if the Act had then applied. In each case, the property is not deferred marital property subject to a surviving spouse's election because the property was acquired before marriage. *See* Wis. Stat. § 851.055.

Assets acquired before a marriage but paid for during a marriage present a potential mixing problem. *See infra* ch. 3.

## **B. Certain Property Acquired During Marriage and After Determination Date [§ 2.111]**

### **1. In General [§ 2.112]**

Certain acquisitions during marriage and after the determination date are individual property if acquired in certain ways. Wis. Stat. § 766.31(7); *see supra* § 2.8 (statutory definition of during marriage). These acquisitions are discussed in sections 2.113–.121, *infra*.

## 2. Gift or Disposition at Death Made to One Spouse by Third Person [§ 2.113]

### a. In General [§ 2.114]

A gift during lifetime or a disposition at death made by a third person to only one spouse during that spouse's marriage and after the determination date is individual property. Wis. Stat. § 766.31(7)(a). Similarly, a distribution of principal or income to one spouse during marriage and after the determination date from a trust created by a third person is the recipient's individual property unless the trust provides otherwise. *Id.* A gift made by a third person to both spouses exclusively as joint tenants or tenants in common during marriage and after the determination date is survivorship marital property or marital property, respectively, unless the donor provides otherwise. *See supra* § 2.97 (discussing section 766.60(4)(b)2.).

➤ **Note.** The definition of during marriage in section 766.01(8) does not include periods when either or both of the spouses are not domiciled in Wisconsin. Distributions and gifts like those described in this section are not subject to the Act if they occur while either or both of the spouses are not domiciled in Wisconsin. If both spouses are domiciled in Wisconsin after receiving a gift from a third party, the property could be reclassified by marital property agreement or other means provided by the Act.

### b. Outright Gift [§ 2.115]

An outright gift is individual property within the terms of section 766.31(7)(a) if it is made by a third person to only one spouse during marriage and after the determination date. *See supra* § 2.8 (statutory definition of during marriage). Section 766.31(7)(a) does not refer to gifts made by one spouse to the other. Section 766.31(10), however, permits spouses to reclassify their property by gift. *See infra* §§ 2.286–.288.

Of course, a gift must in fact have been made. For example, what may appear to be a testamentary gift may actually be the fulfillment of a contractual obligation. In *Andrews v. Andrews*, 199 P. 981 (Wash. 1921), the court determined that a testamentary devise was, in reality,

given in exchange for services to the decedent and thus was community property rather than the separate property of the purported devisee. To further illustrate, an inter vivos transfer from a third person to a spouse for less than adequate consideration may be part gift and part sale; whether the sale portion is marital property or individual property turns on the source of the payment made by the recipient. *See, e.g., Stanger v. Stanger*, 571 P.2d 1126 (Idaho 1977). As a third example, amounts received pursuant to rights compromised in a will contest probably take the same character as the rights compromised. *See, e.g., In re Estate of Clark*, 271 P. 542 (Cal. Ct. App. 1928).

### **c. Distributions from Trust [§ 2.116]**

UMPA has no provisions regarding the classification of distributions from a trust. By contrast, section 766.31(7)(a) provides that a distribution during marriage and after the determination date to one spouse from a trust created by a third party is the individual property of that spouse unless the trust provides otherwise. *See supra* § 2.8 (statutory definition of during marriage).

➤ **Comment.** The scope of section 766.31(7)(a) is not limited to trusts for one spouse only; it also includes trusts created by third parties that could distribute income or principal to either or both of the spouses. However, a distribution from such a trust is the recipient's individual property (unless the trust provides otherwise) if made only in that spouse's name. The policy here is to treat a distribution to one spouse as a gift from a third person to that spouse at the time of distribution. By contrast, a postdetermination date distribution to both spouses jointly or as tenants in common presumably is survivorship marital property or marital property unless the trust provides otherwise. *See* Wis. Stat. § 766.60(4)(b)2.

The word *distribution* includes distributions of both income and principal. *See* Wis. Stat. § 766.31(7)(a). It should make no difference whether a distribution is mandatory or discretionary or whether the recipient spouse is also the sole trustee or a cotrustee of the trust making the distribution. It is probably irrelevant whether an amount received through the exercise of a power of withdrawal is a distribution; receipt of such an amount is virtually the same as receipt of a direct gift from a third person and should therefore be considered the recipient's individual property unless the trust provides otherwise.

➤ **Note.** Income accumulated inside a trust created by a third party is not income within the definition of section 766.01(10) while it remains in the trust; this should be true even of income subject to a power of withdrawal. Section 766.01(10) (defining *income*) applies to trusts created for a spouse by a third party. A different result appears to be required in connection with certain trusts created by a spouse for his or her own benefit. *See supra* §§ 2.98–.104.

### **3. Property Received in Exchange for or with Proceeds of Individual Property: Tracing to Individual Property [§ 2.117]**

If the source of payment for an asset acquired by a spouse during marriage and after the determination date can be traced to assets classified as individual property, the asset acquired is individual property. Wis. Stat. § 766.31(7)(b); *see supra* § 2.8 (statutory definition of during marriage). Similarly, if an asset is mixed, tracing to the individual property component preserves that component's individual property character. Wis. Stat. § 766.63(1); *see also infra* ch. 3 (tracing); *Wierman v. Wierman*, 130 Wis. 2d 425, 387 N.W.2d 744 (1986) (tracing used in dissolution context).

### **4. Appreciation of Individual Property [§ 2.118]**

Appreciation of a spouse's individual property asset during marriage and after the determination date is individual property except to the extent that the appreciation is classified as marital property under section 766.63 (pertaining to mixed property). Wis. Stat. § 766.31(7)(c); *see supra* § 2.8 (statutory definition of during marriage). Substantial appreciation of either spouse's property other than marital property attributable to the substantial undercompensated labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity (hereinafter often referred to as *efforts*) of *either* spouse in connection with that property is marital property resulting in a mixed asset. Wis. Stat. § 766.63(2); *see infra* §§ 3.45–.48. All other appreciation is individual property, however, including appreciation resulting from market conditions and spousal efforts when all the tests of section 766.63(2) are not met, *see infra* § 3.45. UMPA § 4 cmt.

➤ **Example.** Suppose that during marriage and after the determination date a wife inherits a parcel of vacant real estate (individual property). If neither the wife nor her husband applies substantial efforts to the property but the property quadruples in value during marriage, the appreciation is the wife's individual property. *Id.*

## **5. Property Acquired by Gift, Unilateral Statement, Marital Property Agreement, Decree, or Written Consent Classifying Property as Individual**

### **[§ 2.119]**

Section 766.31(7)(d) provides that individual property assets may be acquired by a reclassification by interspousal gift under section 766.31(10). *See infra* §§ 2.286–288. The income from the property is the donee spouse's individual property unless a contrary intent of the donor is established. Wis. Stat. § 766.31(10). Income attributable to a spouse's nonmarital property may be classified as that spouse's individual property assets if he or she executes a unilateral statement. *Id.*; *see supra* § 2.71. Individual property assets may also be acquired by a marital property agreement. Wis. Stat. § 766.31(7)(d).

Section 766.31(7)(d) further provides that individual property assets may be acquired during marriage and after the determination date “by a decree.” *See* Wis. Stat. § 766.01(3) (defining *decree*); *see also supra* § 2.8 (statutory definition of during marriage). Section 766.31(7)(d) does not identify or define the types of court decrees that are included. However, other provisions of the Act authorize a number of different types of decrees, including the following:

1. If marital property has been or is likely to be substantially injured by a spouse's gross mismanagement, waste, or absence, a court may order that the classification of an existing marital property asset be changed, Wis. Stat. § 766.70(4)(a)2., or that property acquired by either spouse after the court order is the acquiring spouse's individual property, Wis. Stat. § 766.70(4)(a)5.; *see infra* § 8.31.
2. A court may order that a spouse's recovery for damage to property under section 766.70 be classified as other than individual property. *See* Wis. Stat. § 766.31(7)(e); *see also infra* § 8.38.

3. A court may issue a decree determining the classification of previously acquired property as part of a probate proceeding, Wis. Stat. § 857.01, or during marriage, Wis. Stat. § 766.70(2).
4. A decree itemizing a personal-injury recovery acquired during marriage and after the determination date may allocate a portion to pain and suffering (which is individual property) and a portion to earnings lost during marriage (which is marital property). *See* Wis. Stat. § 766.31(7)(f); *see also infra* § 4.52 (whether uninjured spouse must be party). (If the recovery is not classified, it may be classified entirely as marital property because of the presumption under section 766.31(2).)

Spouses may use a written consent to reclassify life insurance policies and property used to pay premiums on such policies, or both, under section 766.61(3)(e). Wis. Stat. § 766.31(10); *see infra* § 2.177.

➤ **Historical Note.** Section 766.31(7)(d) originally provided that individual property assets could be acquired by written consent. This provision was eliminated by the 1985 Trailer Bill. The elimination of written consent as a means by which spouses could reclassify property other than certain insurance policies and property used to pay premiums on those policies reflected concern that a written consent could act as a substitute for a marital property agreement, without the disclosure and other requirements of a marital property agreement. *See* Wis. Stat. Ann. § 766.31(7)(d) Legis. Council Notes—1985 Act 37, §§ 76 to 83 (West 2009). Subsequently, the 1988 Trailer Bill expanded the scope of written consents so that they may be used to reclassify all life insurance policies and proceeds and assets used to pay premiums on those policies. *See* Wis. Stat. § 766.61(3)(e).

For planning purposes, written consents are useful for designating beneficiaries of life insurance policies and relinquishing or reclassifying interests in life insurance policies and assets used to pay premiums on those policies. *See infra* §§ 2.177, 10.187, .188. Consents, written or oral, may also be useful in connection with gifts to third parties. Although the Act does not so state, a consent satisfies the “acting together” requirement of section 766.53: that is, a spouse could give marital property to a third party, and the other spouse could subsequently give consent. The consent is deemed effective as of the date of the transfer. *See* Wis. Stat. Ann. § 766.53 Legis. Council Committee

Supplemental Notes Relating to 1985 Act 37 (West 2009); *see also infra* § 4.35.

## **6. Individual Recoveries Under Section 766.70**

### **[§ 2.120]**

The general rule is that a recovery to a spouse under section 766.70 during marriage and after the determination date for damages to that spouse's property is that spouse's individual property except as specifically provided otherwise in a decree or marital property agreement. Wis. Stat. § 766.31(7)(e). Section 766.70 creates various interspousal and other remedies, *see infra* ch. 8, some of which redress damage to one spouse's property caused by the other spouse's wrongful conduct. That the recovery is individual property is apparently a manifestation of the rule that a tortfeasor spouse should not profit from his or her wrong. *See infra* § 2.134. But cases are envisioned under section 766.70 that would give rise to recoveries that are marital property, and thus each remedy for damages (as opposed to other remedies) in section 766.70 should be examined.

Under section 766.70(1), a spouse may recover for damages to his or her property (of any classification) caused by the other spouse's breach of the good-faith duty set forth in section 766.15(1). An important issue is whether one spouse's negligent conduct resulting in damages to the other spouse's property is a breach of the good-faith duty and, if not, whether the rule that tortfeasors should not profit from their wrongs would be applied in any event. *See infra* §§ 2.134, 8.18.

Under section 766.70(5), when marital property is used to satisfy obligations other than support or family-purpose obligations, the nonobligated spouse may request a court to order that he or she receive as individual property the amount of marital property needed to equal in value the marital property used to satisfy the obligation, subject to certain third-party rights and equitable considerations. *See infra* § 8.36.

For discussion of rights of recovery one spouse has against the other and classification of recoveries in connection with certain gifts to third parties, see sections 8.44–.59, *infra*.



## **7. Recoveries for Personal Injury [§ 2.121]**

Recoveries for personal injury, amounts attributable to expenses paid or otherwise satisfied from marital property funds, and amounts attributable to loss of income during marriage and before and after the period defined by the Act as during marriage are considered in sections 2.127–.134, *infra*.

## **VIII. Certain Recoveries and Income Substitutes [§ 2.122]**

### **A. In General [§ 2.123]**

To complete the categories of marital and individual property, it is useful to group various types of recoveries and income substitutes.

### **B. Insurance Recoveries and Recoveries for Damage to Property [§ 2.124]**

#### **1. Damages Caused by Third Party; Judgments and Insurance [§ 2.125]**

Damages received for injury to property caused by third parties have the same classification as the damaged property. *See* Reppy & Samuel, *supra* § 2.19, at 166. Thus, damages for injury to marital property assets are marital property because that result is consistent with the nature of the property and tracing rules. Damages received for injury to assets classified as individual property are individual property because that result is consistent with the nature of the property and the tracing rules in sections 766.31(7)(b) and 766.63(1). Consistent with the nature of the property and section 766.63(1), which provides for tracing to nonmarital property, and section 766.31(8), which provides for tracing to predetermination date property, damages received for injury to predetermination date property should take the same character as the predetermination date asset.

In the other community property states, most courts have held that an insurance recovery takes the character of the underlying property interest protected. Reppy & Samuel, *supra* § 2.19, at 166. Thus, an insurance recovery received for damage to a marital property asset is marital

property; an insurance recovery received for damage to an individual property asset is individual property; an insurance recovery received for damage to predetermination date property is predetermination date property.

➤ **Comment.** Occasionally, a court will trace the funds used to purchase the insurance and classify the recovery accordingly. *See, e.g., Russell v. Williams*, 374 P.2d 827 (Cal. 1962). Care should be exercised before that rule is adopted in Wisconsin because it undercuts the purpose of the insurance policy and may produce a windfall to the marital, individual, or predetermination date “estate” that paid the premium. A right of reimbursement for premiums paid may be sufficient. *See Trahan v. Trahan*, 387 So. 2d 35 (La. Ct. App. 1980); *see also infra* § 3.29.

## **2. Damages Caused by Spouse [§ 2.126]**

For a discussion of damages received for injury to property caused by a spouse, see section 2.120, *supra*, and section 2.134, *infra*.

## **C. Personal-injury Recoveries [§ 2.127]**

### **1. In General [§ 2.128]**

Awards for personal injury often involve damages for pain and suffering, reimbursement for expenses paid, and compensation for lost income. Section 766.31(7)(intro.) and subsection (f) are relevant and must be read together as follows:

(7) Property acquired by a spouse during marriage and after the determination date is individual property if acquired by any of the following means:

....

(f) As a recovery for personal injury except for the amount of that recovery attributable to expenses paid or otherwise satisfied from marital property and except for the amount attributable to loss of income during marriage.

A recovery by a spouse for pain and suffering during marriage and after the determination date, therefore, is always individual property.

Income earned on that kind of recovery is marital property unless subject to a unilateral statement or other applicable exception described in section 2.69, *supra*.

A recovery for expenses paid or otherwise satisfied from marital property is marital property. It may be inferred that a recovery for expenses paid or otherwise satisfied from nonmarital property (even predetermination date property) is individual property because of the interrelationship between the introductory portion of section 766.31(7) and subsection (f). On the other hand, it is arguable that a recovery of an expenditure should be of the same classification as the source that paid it. *See infra* § 3.29.

A recovery for loss of income requires examination. Before undertaking that examination, it is necessary to understand the significance of the term during marriage under the Act. Subsection (f) of section 766.31(7) indicates that an amount recovered that is attributable to loss of income “during marriage” is not individual property (and therefore is marital property). Subsection (f) makes no reference to the determination date; that is not a matter of significance. The term during marriage as defined in section 766.01(8) means a period in which both spouses are domiciled in Wisconsin, which begins at the determination date and ends at dissolution or at the death of a spouse. Implicit in the definition is that the period during marriage ends if one or both of the spouses are no longer domiciled in the state. During such a period, the Act does not apply.

➤ **Note on Terminology.** The term during marriage as used in this chapter should be understood to mean “during marriage as defined by the Act.” The statutory phrase “during marriage and after the determination date” is used throughout sections 2.129–.134, *infra*, but it should be noted that, in view of the definition of during marriage, the words “and after the determination date” are redundant.

Consistent with section 766.31(4) and the definition of during marriage, a recovery for loss of income should be marital property only if it replaces income that would have been earned or accrued by a spouse during marriage and after the determination date; otherwise, it is not marital property. In addition, the implication in section 766.31(7)(f) is that a recovery for lost income must be apportioned between the amount lost during marriage and the amount lost before or after the period defined as during marriage.

➤ **Note.** Unlike statutes in at least two community property states, section 766.31(7)(f) refers to a “recovery” rather than to the accrual of a cause of action, *see* La. Civ. Code Ann. art. 2344 (West, WESTLAW current through the 2009 Regular Session); Cal. Fam. Code § 781 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009–2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 19 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot); *see also infra* § 4.49. Moreover, it refers to a “recovery” acquired “during” marriage; nothing in the Act expressly refers to recoveries acquired before or after the period defined as during marriage. Section 766.31 also differs from UMPA’s “wait-and-see” rule. *See infra* § 2.133.

For a discussion of punitive damages recovered by a spouse from a third party, *see* Scott A. Hennis, *Punitive Damages: Community Property, Separate Property or Both*, Community Prop. J., Apr. 1987, at 51.

## 2. Injury and Recovery Before Period Defined as During Marriage [§ 2.129]

➤ **Example.** Suppose that in 1990, a man is injured and acquires a recovery for personal injury, including a sum for future lost wages. The man subsequently marries. Both spouses are domiciled in Wisconsin at the date of their marriage. Can his wife successfully claim that some portion of the award her husband obtained while he was single was designed to compensate for loss of income during marriage and after the determination date and that, therefore, she is entitled to a portion of the recovery? It appears that the answer is no. The recovery was not obtained during marriage, and so section 766.31(7) does not apply; rather, the recovery was property the husband brought to the marriage. It should, therefore, be his individual property under section 766.31(6). On the other hand, a policy argument could be made that earnings replacements should be classified as marital or individual property, based on the earnings they are intended to replace, so that to the extent a recovery compensates for future wages lost during marriage, it should be classified as marital property.

### 3. Injury Before Period Defined as During Marriage; Recovery During Marriage [§ 2.130]

➤ **Example 1.** Assume that a man is injured before January 1, 1986, marries after January 1, 1986, and acquires a recovery during marriage for pain and suffering and loss of income from the injury. Assume that a portion of the recovery is attributable to loss of income during marriage, and a portion to loss of income before the man married. Section 766.31(7)(f) applies because the recovery was acquired during marriage and after the determination date. The portion of the award attributable to income lost before the marriage is the husband's individual property because it is not attributable to loss of income during marriage and after the determination date. The portion for pain and suffering is likewise the husband's individual property. However, that portion of the recovery attributable to income lost during marriage and after the determination date is marital property pursuant to the last clause of section 766.31(7)(f) and the basic rule of section 766.31(1) that all property of spouses is marital property unless classified otherwise.

➤ **Example 2.** Assume the facts in Example 1 above are changed so that the man is injured after his marriage but while either he or his wife is domiciled in a state other than Wisconsin and that the man acquires a recovery when both spouses are domiciled in Wisconsin. In this example, the injury occurs during a period preceding that defined as during marriage in section 766.01(8). Recovery, however, is acquired during marriage (as that term is defined in section 766.01(8)) and after the determination date. Presumably, the recovery that replaces income attributable to income lost while either the husband or the wife was domiciled in a state other than Wisconsin is the husband's nonmarital property because it is not attributable to loss of income during marriage. However, the recovery is deferred marital property subject to election under section 861.02 if the wife survives her husband and the husband is domiciled in Wisconsin at the time of his death still owning that income or assets traceable to it. The portion for pain and suffering is the husband's individual property. The portion of the recovery attributable to income lost during the period after the determination date while both spouses were domiciled in Wisconsin (that is to say, during marriage and after the determination date) is marital property pursuant to the last clause

of section 766.31(7)(f) and the basic rule of section 766.31(1) that all property of spouses is marital property unless classified otherwise.

#### 4. Injury and Recovery During Marriage [§ 2.131]

➤ *Example.* Assume that a spouse is injured and acquires a recovery during marriage. Only the portion of the recovery attributable to loss of income during marriage and after the determination date and to expenses paid or otherwise satisfied from marital property funds is marital property. Wis. Stat. § 766.31(7)(f).

After a recovery is acquired, the period defined as during marriage may end because of death or dissolution or because one or both of the spouses are not domiciled in Wisconsin. Section 766.31(7)(f) implies that the portion of a recovery attributable to loss of income after the end of the period defined as during marriage is not marital property. This notion is consistent with the worker's compensation cases cited in section 2.132, *infra*, in the event of a dissolution. Division of such a recovery at dissolution is a chapter 767 issue. See also the rules of section 766.31(7m), applicable when the uninjured spouse predeceases the injured spouse, and the discussion in section 2.133, *infra*.

Section 766.31(7)(f) does not distinguish between lump-sum awards and awards payable over time. Although payments over time are easier to apportion after the period defined as during marriage has ended, it is certainly possible that a portion of an installment payment, even that received after the period during marriage has ended, was designed to compensate for loss of income during marriage. Moreover, a lump-sum award might very well be designed to compensate for income lost in the future, as well as that lost in the past.

The experience in Louisiana may be of interest. In *Hall v. Hall*, 349 So. 2d 1349 (La. Ct. App. 1977), a husband acquired a judgment for personal injury during marriage. The settlement was paid in full to the husband 10 days before the dissolution of the marriage. The judgment was designed to compensate, in part, for future lost wages. The husband claimed that the judgment for lost wages after dissolution should be his separate property. The court disagreed, saying it could find no positive statement in the Louisiana statutes providing an exception for that kind of property from the general rule that property acquired during marriage is community property.

Referring to *Hall*, a commentator states:

The legislature responded in 1980 with a proviso that “[i]f the community regime is terminated otherwise than by death of the injured spouse, the portion of the damages attributable to the loss of earnings that would have accrued after the termination of the community property regime is the separate property of the injured spouse.”

Reppy & Samuel, *supra* § 2.19, at 175; *see* La. Civ. Code Ann. art. 2344 (West, WESTLAW current through the 2009 Regular Session).

A lump-sum award acquired during marriage is individual property except to the extent of the last clause in section 766.31(7)(f), which creates an exception for an amount attributable to loss of income during marriage. This last clause implies that a settlement must be apportioned on an annual basis to determine which portion represents loss of income during marriage and which does not. Of course, it is helpful to set forth in a court decree or settlement document the period of time involved in any recovery of lost income so that it might be more easily apportioned, if necessary, after the recovery is acquired. Unless the award itself spells out a computation method applicable to such an eventuality, a court, striving for simplicity and applying the general presumption that property of a spouse is marital property, might treat a lump-sum award acquired during marriage and after the determination date as entirely marital property.

Two examples comparing an award payable in installments with a lump-sum award may be helpful.

➤ **Example 1.** Assume that a settlement specifies that \$200,000 of a particular award, payable in equal annual installments, is to compensate for income that will be lost over the next 20 years and that the award is payable in full regardless of the injured spouse’s death or the dissolution of the marriage. As each year elapses during marriage, 1/20 of the award is marital property; it will not be known what classification attaches to future installments of the award until they are paid. If the spouses divorce after 15 years of payments have been received, the \$150,000 of the award already received is marital property, and the \$50,000 yet to be paid is the injured spouse’s nonmarital property because it represents loss of future income that will not be received during marriage. However, the nonmarital portion is subject to division at dissolution if equitable principles

require. *See infra* § 2.132. If the uninjured spouse dies after 15 years of payments have been received, that spouse's marital property interest in the remaining \$50,000 of the award terminates. Wis. Stat. § 766.31(7m); *see infra* § 2.133.

If the injured spouse dies after 15 years of payments survived by the uninjured spouse, a question arises. On the one hand, the \$50,000 yet to be paid was designed to replace lost income regardless of the date of death. That income would have been lost during marriage but for the injured spouse's death, and, thus the surviving spouse should have a marital property interest in it. On the other hand, under a literal reading of section 766.31(7)(f), it is arguable that the \$50,000 yet to be paid cannot represent income lost during marriage and must be the deceased spouse's solely owned property.

➤ **Example 2.** Assume the same facts as in Example 1 above, but assume that the award is a lump sum. To the extent that the \$50,000 representing the income for the final five years can be traced, it is arguable that the analysis should be the same as in Example 1. For simplicity's sake, however, it is arguable that marital status (and the spouses' domicile) on the date of recovery of the award should be determinative (although that argument conflicts with a literal analysis), when the time period in connection with lost income is not specified.

Awards are susceptible to mixing problems after receipt, but tracing should be available. *See Devlin v. Devlin*, 189 Cal. Rptr. 1 (Ct. App. 1982).

## **5. Injury During Marriage; Recovery After Period Defined as During Marriage [§ 2.132]**

➤ **Example 1.** Assume that a husband is injured during marriage, but he (or his estate) recovers damages after the termination of the period defined as during marriage. A portion of the award is attributable to income lost during marriage and after the determination date. In that case, although the cause of action accrues during marriage, the recovery is not obtained at that time. Therefore, section 766.31(7)(f), which refers only to recoveries acquired during marriage, does not apply.



The Act does not expressly deal with the situation in the above example. Two cases, one decided in Washington and the other by the Wisconsin Supreme Court under pre-Act law, may offer some guidance. It should be noted that both cases hold that a personal-injury claim that has not been reduced to settlement or judgment before a dissolution is nevertheless property subject to division.

A sensible approach was adopted in *Brown v. Brown*, 675 P.2d 1207 (Wash. 1984), in which the Washington Supreme Court first overruled prior cases holding that personal-injury awards were community property under Washington statutes. The court held that when an injury occurs before commencement of a dissolution action but recovery has not yet occurred at dissolution, the divorce court should analyze the elements of the potential recovery and categorize them as follows:

1. Damages for physical injury and pain and suffering should be the spouse's separate property.
2. Damages for injury-related expenses should be community or separate property, depending on which fund incurs the expense.
3. Damages for lost wages and diminished earning capacity should have the same community or separate character as the wages and earning capacity they are intended to reimburse.

Following those principles, the court held that compensation for lost wages and diminished earning capacity is community property to the extent the recovery replaces income that would have been earned during the marriage but for the injury; and the portion of a recovery that compensates the injured spouse for wages that would have been earned after separation is that spouse's separate property. Although Washington treats the community as terminated at the date of separation rather than at dissolution, whereas Wisconsin treats marital property as continuing to accrue until dissolution, *Brown* nevertheless provides a useful analysis. *Brown* also provides a review of the treatment of personal-injury recoveries in the various community property states.

In *Richardson v. Richardson*, 139 Wis. 2d 778, 407 N.W.2d 231 (1987), the wife brought a claim for medical malpractice before the commencement of dissolution proceedings. The Wisconsin Supreme Court affirmed the holding of the court of appeals that a personal-injury claim is property subject to division at dissolution under section 767.61.

The claim, said the court, should be divided into its various elements when determining whether the presumption of equal distribution established in section 767.61 applies. The court concluded that a circuit court should presume the following:

1. The injured spouse is entitled to (a) the amount recovered for loss of bodily function and pain and suffering and (b) the entire amount recovered for loss of future earnings after the date of dissolution.
2. The uninjured spouse is entitled to the entire amount recovered for loss of consortium.
3. Amounts recovered for medical and other expenses incurred during marriage and amounts recovered for loss of earnings during marriage are to be distributed equally.

The court in *Krebs v. Krebs*, 148 Wis. 2d 51, 435 N.W.2d 240 (1989), followed the logic of *Richardson* to a similar conclusion. *Richardson* and *Krebs* were dissolution proceedings. Neither dealt with classification issues under the Act; thus, equitable principles applicable to dissolution are not relevant to an analysis under the Act. However, the division of the award into its elements could be relevant for future cases dealing with classification of personal-injury claims under the Act.

Two cases from other jurisdictions involving worker's compensation recoveries that occurred during marriage but were to be paid in part after dissolution came to conclusions similar to those in *Richardson* and *Krebs*. They treated the portion of the award attributable to earnings lost during marriage as community property but the portion attributable to earnings after dissolution as the recipient's separate property. See *Bugh v. Bugh*, 608 P.2d 329 (Ariz. Ct. App. 1980); *Cook v. Cook*, 637 P.2d 799 (Idaho 1981).

➤ **Example 2.** Assume that Example 1 above is changed so that the husband acquires the recovery while the spouses are married but at a time when one of them is not domiciled in Wisconsin. Subsequently, both are domiciled in this state, and then the husband dies survived by his wife. The recovery was not acquired during marriage as defined by the Act; thus, section 766.31(7)(f) does not apply. Is the recovery deferred marital property if the husband dies domiciled in Wisconsin still owning assets traceable to the recovery that compensated for income lost while the spouses were married? The answer should be

yes, because the amount that replaces income lost while spouses are married to each other but during a period when one or both of the spouses are not domiciled in Wisconsin meets the definition of deferred marital property. *See* Wis. Stat. § 851.055; *see also infra* § 2.221.

As previously stated, recovery after dissolution is a property right subject to division. Therefore, if the decree does not deal with the recovery, the parties may own the former marital property portion of the recovery as equal tenants in common. Wis. Stat. § 766.75.

## **6. Terminable Interest [§ 2.133]**

The uninjured spouse's marital property interest in a recovery for loss of income is similar to a terminable marital property interest in a deferred-employment-benefit plan. *See infra* § 2.201.

➤ **Example.** Assume that a spouse is injured during marriage and acquires a recovery for loss of income during marriage and after the determination date. Assume that the uninjured spouse predeceases the spouse who acquired the recovery. Section 766.31(7m) provides that insofar as marital property includes damages for loss of future income arising from the surviving spouse's personal-injury claim, the surviving spouse is entitled to receive as his or her individual property that portion of the award that represents an income substitute after the uninjured spouse's death. The portion of the award that represents income lost before the uninjured spouse's death during marriage and after the determination date is marital property.

Because section 766.31(7m) refers to damages, the section may not apply to disability insurance payments from a policy owned by a spouse. However, results similar to those required by section 766.31(7m) may obtain in any event. *See infra* § 2.136.

➤ **Note.** The Act did not adopt UMPA's wait-and-see provisions on personal injuries in the context of deferred marital property. Section 4(g)(6) of UMPA classifies all personal-injury recoveries as individual property, except portions allocable to expenses paid from marital property funds. At death or dissolution, UMPA's deferred marital property provisions treat any portion of a personal-injury

recovery that can be traced to a loss of earning capacity during marriage as if it were marital property. *See* UMPA §§ 17(2), 18(b).

## 7. Recovery from Tortfeasor Spouse [§ 2.134]

Wisconsin does not recognize interspousal immunity. Wis. Stat. § 766.97(2). How is a recovery of one spouse from the other classified? The Act provides no explicit guidance.

➤ *Example.* A husband and wife are traveling in an automobile. The husband is negligent, resulting in an accident that injures the wife, and she recovers an award from the husband's insurance company. A portion of the award is allocated to the loss of income that she otherwise would have earned from employment during marriage.

In *Freehe v. Freehe*, 500 P.2d 771 (Wash. 1972), *overruled on other grounds by Brown v. Brown*, 675 P.2d 1207 (Wash. 1984), *Flores v. Flores*, 506 P.2d 345 (N.M. Ct. App. 1973), and *Rogers v. Yellowstone Park Co.*, 539 P.2d 566 (Idaho 1975), which involved situations similar to that in the above example, the rule was adopted that the victim spouse could recover as his or her separate property one-half the general damages for loss of earnings that would otherwise have been community property, on the theory that a tortfeasor should not profit from his or her wrongful conduct. Section 766.31(7)(e), dealing with damages to a spouse's property by the other spouse, may suggest a similar result. *See infra* § 8.38.

*Smith v. State Farm & Casualty Co.*, 192 Wis. 2d 322, 531 N.W.2d 376 (Ct. App. 1995), may be of interest. That case involved the death of the spouses' son, which resulted in part from the husband's contributory negligence. The issue was whether the husband's negligence could be imputed to the wife, thereby reducing her award under the Wisconsin wrongful-death statute. The defendant argued that the recovery was marital property and that a recovery would therefore benefit the husband in part. The court rejected this argument, saying that the Act does not limit an innocent spouse's recovery in a wrongful-death action.

The *Smith* court relied on *Chang v. State Farm Mutual Automobile Insurance Co.*, 182 Wis. 2d 549, 514 N.W.2d 399 (1994), which made no reference to the Act, and which held that a nonnegligent parent is

entitled to a full recovery despite a spouse's negligence. The decision in *Smith* did not analyze whether the recovery is marital property, nor did it focus on the rule that a tortfeasor should not benefit from his or her own wrong. Rather, the court felt that the recent decision in *Chang* set a powerful precedent that should be followed. *Smith*, 193 Wis. 2d at 336. In fact, if the recovery is not marital property, the issue whether a tortfeasor can benefit from his or her own wrong drops out of the case. The recovery in *Smith* may well have been individual property because an award under a wrongful-death statute is individual property except for reimbursement of expenses paid from marital property, *see infra* § 2.137. A recovery for personal injury is also individual property except to the extent the recovery is for loss of income during marriage or reimbursement of expenses paid from marital property. *See supra* § 2.128.

## **D. Other Recoveries [§ 2.135]**

### **1. Disability Payments [§ 2.136]**

Disability payments fall into two general categories: those that are connected with deferred-employment-benefit plans and those that are not. Payments made from a deferred-employment-benefit plan representing a right to compensation for loss of income during disability are included within the definition of a deferred-employment-benefit plan, Wis. Stat. § 766.01(4)(b)3., and are subject to the classification rules of section 766.62. *See infra* § 2.191.

When considering the application of section 766.62(2) (dealing with classification of mixed property deferred employment benefits) to a plan involving disability payments, a question arises: When does the plan commence? Is it from the moment coverage begins or from the date of the injury?

➤ **Example.** Assume that an employee becomes a member of a plan that provides, among other benefits, compensation for loss of income during disability. The employee begins participation in the plan five years before the determination date. Three years after the determination date, the employee is disabled, ceases employment, and receives \$10,000 as compensation for loss of income during disability. Assume that at all relevant times the employee and the

employee's spouse are domiciled in Wisconsin. It may be argued that the plan actually begins when the injury occurs. The argument is that since the definition of a deferred-employment-benefit plan in section 766.01(4) does not include various types of insurance benefits "except to the extent that benefits under the plan ... [r]epresent a right to compensation for loss of income during disability," payments for disability are not a plan until injury occurs and a right to compensation accrues. *See* Wis. Stat. § 766.01(4)(b)3. If that is the case, the \$10,000 is entirely marital property because it represents income lost during marriage. *See supra* § 2.8 (statutory definition of during marriage). This argument is consistent with the nature of a plan that compensates for the loss of future income.

On the other hand, the provisions of section 766.01(4)(b)3. modify the words "benefits under the plan." Typically, disability benefits are paid in connection with a plan offering an employee a variety of benefits, only one of which is payment for disability should it occur. Under this view, the plan referred to commences on the day the employee becomes a participant in the overall plan and begins to earn all the benefits under it. The result of this analysis is that 5/8 of the \$10,000 is nonmarital property and 3/8 is marital property.

Classification of other types of disability payments (usually made from policies purchased by a spouse) are treated differently. Some courts hold that disability payments that compensate for pain and suffering are separate property. *See In re Marriage of Mueller*, 137 Cal. Rptr. 129 (Ct. App. 1977); *In re Marriage of Kittleson*, 585 P.2d 167 (Wash. Ct. App. 1978); *see also Leighton v. Leighton*, 81 Wis.2d 620, 261 N.W.2d 457 (1978) (holding that veteran's federal disability pension was compensation for bodily impairment and could not be divided at divorce).

Compensation for lost income from a disability policy, on the other hand, is marital property if it replaces income lost during marriage and after the determination date under the general principles of subsections 766.31(4) and (1). To the extent disability payments replace earnings lost after termination of the period defined as during marriage, the disability payments should be treated as the recipient's nonmarital property.

Whether the source of the premium payment is marital property funds or nonmarital property funds should not be relevant because of the

definition of income in section 766.01(10). As defined in that section, income includes proceeds (other than death benefits) received from a disability insurance policy or any plan, fund, program, or other arrangement providing benefits similar to that form of insurance. Under section 766.31(4), income of all types and regardless of source (unless subject to a unilateral statement, marital property agreement, or other exception described in section 2.69, *supra*) is marital property to the extent it is earned or accrued by a spouse during marriage and after the determination date.

This analysis precludes the type of analysis used in *Elfmont v. Elfmont*, 891 P.2d 136 (Cal. 1995), in which the court, applying California law, explained that if the insured spouse becomes disabled during marriage, the benefits received during marriage are community property. The court said that if benefits continue after the spouses separate, the benefits are separate property of the spouse whose income they replace unless, during marriage, the premiums were paid with community property funds with the intent to provide retirement income. If, however, the insured spouse does not become disabled during the last policy term for which the premium was paid before the parties' separation, the community will have no interest in the benefits produced by renewals of the policy for subsequent terms, because the renewal premium will not have been paid during marriage with community funds and with the intent of providing community retirement income. But see *In re Marriage of Brewer*, 949 P.2d 404 (Wash. Ct. App. 1998), in which the court "reluctantly" held that because all premiums were paid from community funds, the disability benefits received after dissolution by the insured spouse were all community property even though no retirement element was involved.

## **2. Wrongful-death Proceeds [§ 2.137]**

It has been stated that in community property jurisdictions, wrongful-death proceeds are treated as community property. See William Q. de Funiak & Michael J. Vaughn, *Principles of Community Property* § 84, at 209 (2d ed. 1971). This would appear not to be true in Wisconsin.

It is true, as one authority points out, that in the case of the wrongful death of a spouse, the community may be injured by the wrongful death to the extent of deprivation of the deceased spouse's earnings or services for the period of that spouse's normal life expectancy. See *id.* Pecuniary

loss of this type is the major element of damages under the Wisconsin wrongful-death statute. *See* Wis. Stat. § 895.04(4). Nonetheless, a recovery for pecuniary injury arguably should not be classified as marital property for two reasons. First, the wrongful death of a spouse gives rise to a cause of action, but death terminates the marriage, and there can be no marital property after the marriage terminates. Second, the Wisconsin wrongful-death statute vests the recoveries not in the victim's estate (with the exception of certain expenses paid by the estate) but in named beneficiaries. *See* Wis. Stat. § 895.04; *Weiss v. Regent Prop., Ltd.*, 118 Wis. 2d 225, 346 N.W.2d 766 (1984). If this vesting of the recoveries does not create solely owned property in the beneficiaries described in the statute, then presumably a court or the parties must characterize the various wrongful-death recoveries permitted by the statute. These recoveries include pecuniary loss, up to \$500,000 per occurrence in the case of a deceased minor and up to \$350,000 per occurrence for a deceased adult; for loss of society and companionship under section 895.04(4); and various medical and funeral expenses described in section 895.04(5). A court should consider what the award is designed to replace and classify the various recoveries accordingly. *Reppy & Samuel, supra* § 2.19, at 180–81; *see also Smith v. State Farm & Cas. Co.*, 192 Wis. 2d 322, 531 N.W.2d 376 (Ct. App. 1995) (holding that Act does not limit innocent spouse's recovery in wrongful-death action brought as result of other spouse's negligence).

### **3. Worker's Compensation [§ 2.138]**

The Act does not specifically address the subject of worker's compensation, nor are there any Wisconsin cases that deal with that subject in the context of the Act.

In *Bugh*, 608 P.2d 329, the court held that worker's compensation was awarded in lieu of lost wages and not as damages for pain, suffering, and monetary loss caused by the employer. The court held that worker's compensation paid during marriage to compensate for earnings that otherwise would have been paid to and earned by the community during the marriage was community property; worker's compensation paid after the community was dissolved compensated for earnings that otherwise would have been earned by and paid to the injured worker after the marriage ended and therefore should be the worker's separate property.



Other elements of worker's compensation will require classification, such as certain death benefits, Wis. Stat. §§ 102.46–.49, and medical expenses, Wis. Stat. § 102.42. A court should consider what the award is designed to replace and classify the various recoveries accordingly.

#### **4. Recovery for Loss of Consortium [§ 2.139]**

Wisconsin common law allows a spouse to recover for loss of consortium. *Moran v. Quality Aluminum Casting Co.*, 34 Wis. 2d 542, 150 N.W.2d 137 (1967). Section 766.97(3), which abolishes a spouse's common law rights to compel the other spouse's sexual services, specifically states that nothing in its provisions affects a spouse's common law right to consortium or society and companionship. The Act, however, does not specifically classify a recovery for loss of consortium as either marital or individual property.

Texas treats a recovery for loss of consortium as the recipient spouse's separate property. *See Reed Tool Co. v. Copelin*, 610 S.W.2d 736 (Tex. 1980). The general language of a California statute apparently classifies a recovery for loss of consortium as community property. *See* Cal. Fam. Code § 781 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009–2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 19 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot). Nonetheless, the court in *Lantis v. Condon*, 157 Cal. Rptr. 22 (Ct. App. 1979), noted that loss of consortium impairs spousal interests that are wholly separate and distinct from the interests of the other spouse and that a proper solution would be to reclassify damages for this type of injury as separate property.

Dealing with pre-Act law, the Wisconsin Supreme Court in *Richardson v. Richardson*, 139 Wis. 2d 778, 407 N.W.2d 231 (1987), held that in a dissolution proceeding, a circuit court should presume that the uninjured spouse is entitled to the entire amount recovered for loss of consortium. The court's reasoning is consistent with treating a recovery for loss of consortium as the uninjured spouse's individual property.

## IX. Predetermination Date Property [§ 2.140]

### A. Definition [§ 2.141]

Subject to a major exception, this chapter uses the term predetermination date property to refer to all property owned by either or both of the spouses at the determination date. The major exception, which will increase in significance as time passes, involves property owned by a spouse at a marriage occurring after January 1, 1986, if both spouses, at the date of marriage, have a Wisconsin domicile; such property is that spouse's individual property. Wis. Stat. § 766.31(6); *see supra* § 2.110. The determination date is the last to occur of the following: (1) marriage; (2) January 1, 1986; or (3) the date both spouses establish a domicile in this state. Wis. Stat. § 766.01(5). For a discussion of what constitutes a domicile, see section 13.45–48, *infra*. For a discussion of multiple determination dates, see section 2.8, *supra*.

➤ **Note on Terminology.** The comments to UMPA sometimes refer to predetermination date property as property “having any other classification,” meaning property other than marital or individual property, which are both creations of the Act. UMPA § 4 cmt.

The term predetermination date property does not imply a classification all its own. Rather, each predetermination date asset has its own particular incidents of ownership that attached under the law that governed before the determination date and that continue except as altered by the Act. Predetermination date property is not a type of individual property.

Section 766.31(1) clarifies that the classification of marital property does not include assets that are described in section 766.31(8) (i.e., predetermination date property).

Sections 46 and 47 of 2005 Wisconsin Act 216 confirm in a clarifying amendment to section 766.31(6)(a) that property owned by a spouse at a marriage that occurs on the determination date is that spouse's individual property. A marriage can occur on the determination date only if it occurs after January 1, 1986, and both spouses have a Wisconsin domicile at the date of marriage. On the other hand, if the date of marriage precedes the determination date (as for example, a marriage in a common law state before the spouses change domicile to Wisconsin), the

property owned by a spouse at the determination date is unclassified property (predetermination date property).

## **B. Basic Rule [§ 2.142]**

The first clause of section 766.31(8) states the general rule: “Except as provided otherwise in this chapter, the enactment of this chapter does not alter the classification and ownership rights of property acquired before the determination date....”

This provision derives from UMPA section 4. A comment to this UMPA section states the following:

All of the property of a married couple in an adopting state on hand at the determination date would have a particular classification. Certain incidents would already have attached to the manner of ownership. Survivorship would be an incident of jointly held or entireties property.... Trust interests would be regulated by governing instruments. [UMPA] is *not* designed to alter these various incidents of ownership or to reclassify such property.

UMPA § 4 cmt.

## **C. Three Exceptions to Basic Rule [§ 2.143]**

### **1. In General [§ 2.144]**

The opening language of section 766.31(8) states that chapter 766 does not alter the classification and ownership rights of predetermination date property “[e]xcept as provided otherwise in this chapter” (emphasis added). The comment to UMPA section 4 explains that there are three “minor” exceptions to the general rule that ownership rights and classification of predetermination date property are unaltered by UMPA upon arrival of the determination date. The first is the “as-if-individual” rule, the second is the deferred marital property election at death, and the third is the income treatment already described, *see supra* § 2.69, under which income from predetermination date property earned or accrued by a spouse during marriage and after the determination date is marital property, unless one of the exceptions referred to in section 2.69, *supra*, applies. *See supra* § 2.8 (statutory definition of during marriage).

Sections 2.145–.147, *infra*, discuss these three exceptions. Section 2.148, *infra*, offers some examples.

## 2. “As-if-individual” Rule [§ 2.145]

Although predetermination date property is not individual property, UMPA § 4 cmt., section 766.31(9) of the Act provides as follows:

Except as provided otherwise in this chapter and except to the extent it would affect the spouse’s ownership rights in the property existing before the determination date, during marriage the interest of a spouse in property owned immediately before the determination date is treated *as if it were individual property*.

(Emphasis added.) The comment to UMPA section 4 (from which section 766.31 derives) states that section 4 is not a reclassification statute; rather, the section identifies

pre-determination date property that is solely owned as functioning with a “fraternal twin” relationship to individual property under [UMPA]. It is a transitional rule, stated as it is to avoid a direct substantive reclassification of pre-determination date property, but to clarify the functional treatment of it in applying [UMPA].

By its terms, the as-if-individual rule applies only during marriage, *see supra* § 2.8 (statutory definition of during marriage); it does not apply at death or dissolution. When a spouse who owns or retains certain interests in predetermination date property dies and is survived by the other spouse, a deferred marital property election may apply. At dissolution, the property is subject to the rules of section 767.61. Note also that in an equitable proceeding, a court may subject predetermination date property to a surviving spouse’s rights under chapters 852 and 861 if property arrangements are made in fraud of those rights. Wis. Stat. § 861.17.

During marriage, the as-if-individual rule treats predetermination date property as if it were individual property; consequently, all rules pertaining to individual property apply to predetermination date property during marriage unless they would affect the spouse’s ownership rights. This means the owner (usually titled) spouse:

1. Enjoys exclusive rights of management and control under section 766.51(1)(a), (6);
2. May make gifts of the property without regard to the dollar amounts in section 766.53; and
3. May deal with the property without concern about the good-faith duty of section 766.15(1).

For a description of the attributes of individual property, see section 2.108, *supra*.

The as-if-individual rule is itself subject to exceptions. Thus, predetermination date property is treated as if it were individual property “[e]xcept as provided otherwise in [chapter 766] and except to the extent that it would affect the spouse’s ownership rights in the property existing before the determination date.” Wis. Stat. § 766.31(9).

The reference to exceptions in chapter 766 has only historical interest. Before the 1985 Trailer Bill, the deferred marital property rules were contained in chapter 766. The 1985 Trailer Bill moved the deferred marital property rules to chapter 861. In addition, section 766.75 had provisions treating certain predetermination date property as marital property at dissolution before the 1985 Trailer Bill repealed them. *See infra* § 2.146.

The second exception to the as-if-individual rule, which prohibits the rule’s application “to the extent that it would affect the spouse’s ownership rights in the property existing before the determination date,” Wis. Stat. § 766.31(9), is

intended to avoid any interference with actual ownership incidents in property owned prior to the determination date. For example, community property owned prior to the determination date should not be treated functionally as individual property in applying [UMPA]. On the other hand, tenancy in common property could function as if it were individual property under [UMPA’s] provisions with each owner’s undivided interest being treated as though it were individual property.

UMPA § 4 cmt.

Apparently the thinking is that certain types of ownership rights (e.g., those associated with community property brought into Wisconsin) are so totally inconsistent with ownership rights normally associated with individual property that the as-if-individual rule should not apply to them. Tenancy-in-common property, on the other hand, appears to be close enough to individual property to function as individual property. *Id.*

### **3. Deferred Marital Property Election at Death** **[§ 2.146]**

A second exception to the general rule that predetermination date characteristics will not be altered involves the application of the deferred marital property election in connection with the value of certain kinds of predetermination date property owned at death by a Wisconsin domiciled spouse who is survived by the other spouse. Hardly a minor exception, the election has a dramatic impact on spouses with a domicile in Wisconsin and those who later establish a domicile in Wisconsin. UMPA applies deferred marital property concepts at the termination of a marriage by death or dissolution. UMPA §§ 17, 18. In Wisconsin, the deferred marital property election applies only at death; deferred marital property does not exist at dissolution. *See* Wis. Stat. Ann. § 766.75 Legis. Council Notes—1985 Act 37, §§ 141 to 143 (West 2009).

First, a technical point must be noted. The introductory clause of section 766.31(8) uses the words “[e]xcept as provided otherwise in this chapter,” referring to chapter 766. As originally enacted, the Act embedded deferred marital property concepts in chapter 766 as part of sections 766.75(1) (dissolution) and 766.77 (death). Thus, the original deferred marital property concept was clearly an exception found in chapter 766 to the general rule that predetermination date property retains its predetermination date characteristics. The 1985 Trailer Bill repealed sections 766.75(1) and 766.77 and moved the deferred marital property concept to chapters 851 and 861, so that concept applies only at death in connection with the election available to a surviving spouse. Nevertheless, the deferred marital property rule still operates as an exception to the general rule in section 766.31(8) because it is used in connection with an important elective right granted a surviving spouse.

The definition of deferred marital property and the deferred marital property election are given separate and detailed treatment. *See infra* §§ 2.220–.246, ch. 12. At this point, however, it should be noted that the value of predetermination date property that is deferred marital property is potentially subject to a surviving spouse’s deferred marital property election under section 861.02. Deferred marital property is predetermination date property acquired while spouses are married and while chapter 766 does not apply, but that would have been marital property under chapter 766 had chapter 766 applied when the property was acquired. Wis. Stat. § 851.055. The deferred marital property election has important estate planning implications. *See infra* ch. 10.

#### **4. Income Rule [§ 2.147]**

If none of the exceptions referred to in section 2.69, *supra*, applies, income earned or accrued by a spouse during marriage and after the determination date and attributable to predetermination date property is classified as marital property. *See supra* § 2.69; *see also supra* § 2.8 (statutory definition of during marriage). This rule constitutes the third exception to the general rule that ownership rights and classification of predetermination date property are unaltered by the Act.

#### **5. Examples [§ 2.148]**

Three examples may clarify the application of subsections 766.31(8) and (9).

➤ **Example 1.** Assume that while the spouses were married but before the determination date (and thus before chapter 766 applied to the spouses), a husband purchased stock titled in his name and used his wages (a marital property asset if chapter 766 had then applied) for the purchase. During marriage and after the determination date (and assuming no reclassification by means provided by the Act), he owns all of the incidents of ownership in that asset that he would have owned if chapter 766 had never been adopted, except that in the absence of a unilateral statement, a court decree or marital property agreement to the contrary, or an interspousal gift, the dividends generated during marriage and after the determination date are classified as marital property. After the husband’s death, he is survived by his wife. The stock and its dividends accumulated before

the determination date and still owned by the husband at his death are deferred marital property subject to his wife's elective right under section 861.02.

➤ **Example 2.** Assume that the husband in Example 1 purchased the stock with property that would have been individual property rather than marital property had chapter 766 then applied. At death, he can dispose of all the stock and half the dividends earned and accumulated after the determination date free of any elective right; the value of the dividends held by the husband at his death but accumulated before the determination date are in his augmented deferred marital property estate subject to his wife's section 861.02 election. In the absence of a unilateral statement, a court decree or marital property agreement to the contrary, or an interspousal gift, half the dividends held by the husband at his death but accumulated during marriage and after the determination date are owned by his wife.

➤ **Example 3.** Finally, assume that when the husband in Example 1 purchased the stock, he paid for it partially with inherited assets (which would not have been marital property had chapter 766 then applied) and partially with his wages (which would have been marital property had chapter 766 then applied). In this case, the spouses own all the dividends earned during marriage and after the determination date as marital property in the absence of an interspousal gift, a court decree or marital property agreement to the contrary, or a unilateral statement. If the husband dies after the determination date and is survived by his wife, he can dispose of that portion of the stock traceable to the inheritance. The value of the stock purchased by his wages is in his augmented deferred marital property estate subject to his wife's section 861.02 election. He can dispose of half the dividends earned and accumulated after the determination date. The dividends held by him at his death but accumulated before the determination date are subject to his wife's section 861.02 election; and in the absence of a unilateral statement, a court decree or marital property agreement to the contrary, or an interspousal gift, half the dividends held by him at his death but accumulated during marriage and after the determination date are owned by his wife. *See also infra* § 3.11.



## **D. Appreciation [§ 2.149]**

### **1. In General [§ 2.150]**

Three types of appreciation are associated with predetermination date property:

1. Substantial appreciation of predetermination date property resulting from substantial undercompensated efforts of either spouse applied to the predetermination date property during marriage and after the determination date, *see infra* § 2.151; *see also supra* § 2.8 (statutory definition of during marriage);
2. Substantial appreciation of predetermination date property resulting from substantial undercompensated efforts of either spouse applied to the predetermination date property while married and while chapter 766 did not apply, *see infra* § 2.152; and
3. All other types of appreciation of predetermination date property, whether accruing before or after chapter 766 applies, including appreciation resulting from (a) general market conditions and (b) spousal efforts if all the tests of section 766.63(2) are not met, *see infra* §§ 2.153, 3.44.

### **2. Substantial Appreciation Resulting from Spousal Efforts During Marriage and After Determination Date [§ 2.151]**

Section 766.63(2) provides that the application by either spouse of substantial labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity (generally referred to in this chapter as *efforts*) to either spouse's property other than marital property creates marital property if the appreciation is substantial and if reasonable compensation is not received. Consequently, substantial appreciation of either spouse's predetermination date property resulting from substantial undercompensated efforts of either spouse during marriage and after the determination date is marital property. Four conditions must be satisfied. Appreciation of predetermination date property resulting from spousal

efforts during marriage and while chapter 766 applies is marital property whenever all the following are true:

1. The appreciation is substantial.
2. The appreciation is the result of a spouse's efforts.
3. The efforts are substantial.
4. Reasonable compensation is not received for the efforts.

In the absence of reclassification by means provided by the Act, all other appreciation of predetermination date property (including that resulting from market conditions) is not marital property; rather, it is either (1) potentially deferred marital property subject to the surviving spouse's deferred marital property election at the owner's death or (2) predetermination date property that is not deferred marital property. *See infra* §§ 2.152, .153.

➤ **Example.** Assume that a husband domiciled in Wisconsin marries in 1979 and on January 1, 1981, inherits shares of stock in a business from his mother. The husband expends substantial undercompensated effort in the business while married and before chapter 766 applies and also during marriage and after the determination date, and the value of the stock increases substantially because of those efforts. Assume that the husband predeceases his wife on January 1, 2010. The substantial appreciation of the husband's business resulting from his substantial undercompensated efforts during marriage and after the determination date is marital property. For marital property purposes, such appreciation ceases at death. The appreciation resulting from efforts applied while married and before chapter 766 applied is considered in section 2.152, *infra*.

### **3. Substantial Appreciation Resulting from Spousal Efforts While Married and While Chapter 766 Did Not Apply [§ 2.152]**

Substantial appreciation of either spouse's predetermination date property resulting from substantial undercompensated efforts of either spouse applied while married and while chapter 766 did not apply is

deferred marital property subject to the surviving spouse's election at the owner's death if at death all the following are true:

1. The owner has a Wisconsin domicile.
2. The asset (or assets traceable to it) is part of the augmented deferred marital property estate.
3. The owner is survived by his or her spouse.

Such appreciation meets the requirements of section 851.055 because it would have been marital property had chapter 766 applied to the spouses while the effort was expended. *See* Wis. Stat. §§ 851.055, 766.63(2).

➤ **Example.** Assume the facts in the example in section 2.151, *supra*. Assume that at his death the husband has a Wisconsin domicile and owns the stock. If the husband is survived by his spouse (regardless of her domicile at his death), substantial appreciation of the husband's stock is deferred marital property at his death to the extent that the appreciation resulted from his substantial undercompensated efforts applied while married and while chapter 766 did not apply.

Suppose in the example just given that substantial appreciation accrues while chapter 766 applies (that is, during marriage and after the determination date) with respect to the efforts applied while the spouses were married but before chapter 766 applied. Is the appreciation deferred marital property? The question arises because of doubt as to when appreciation is acquired. Section 851.055 states that deferred marital property is property acquired while spouses are married and while chapter 766 does not apply; in the example given, the efforts were expended before chapter 766 applied, but some of the appreciation caused by those efforts accrued after chapter 766 applied. On the one hand, appreciation actually occurred after the determination date. On the other hand, the better view is that the appreciation that accrued while chapter 766 applied is a direct consequence of efforts expended before chapter 766 applied and thus is inherently part of the asset. This view is supported by the labor-mixing rule in section 766.63(2). Section 766.63(2) does not set any time limitations on when appreciation must accrue so as to be marital property if all the conditions of section 766.63(2) are met.

#### 4. Other Appreciation Accruing Before and After Chapter 766 Applies [§ 2.153]

Appreciation of predetermination date property, other than substantial appreciation resulting from substantial undercompensated efforts of either spouse, is treated as if it is inherently part of the asset that produced the appreciation. This is so whether the appreciation accrues before or after chapter 766 applies. If such appreciation (generally that resulting from market conditions but also that resulting from spousal efforts if the conditions described in section 2.151, *supra*, are not met) accrues on predetermination date property that is deferred marital property, then such appreciation is also deferred marital property. If such appreciation accrues on predetermination date property that is not deferred marital property, then such appreciation is not deferred marital property. If the appreciation accrues on mixed property, the appreciation must be apportioned. See *Plachta v. Plachta*, 118 Wis.2d 329, 348 N.W.2d 193 (Ct. App. 1984), and *Wierman v. Wierman*, 130 Wis.2d 425, 387 N.W.2d 744 (1986), cases in which similar reasoning was applied in the dissolution context to appreciation resulting from causes other than spousal efforts.

#### E. Tracing [§ 2.154]

➤ **Example 1.** Assume that a husband owns a predetermination date asset worth \$100,000. During marriage and after the determination date, he sells the asset and reinvests the proceeds in real estate. Is the real estate classified as predetermination date property? The answer is yes, even though the real estate was acquired after the determination date.

Section 766.31(8) provides that enactment of chapter 766 alters neither the classification and ownership rights of property acquired before the determination date nor the classification and ownership rights of property acquired during marriage and after the determination date in exchange for or with the proceeds of property acquired before the determination date. This rule permits tracing. When predetermination date assets are sold, the proceeds are reinvested, and the source of the reinvestment can be traced, the reinvestment retains the source's predetermination date classification and ownership rights.

➤ **Example 2.** Assume that, in Example 1 above, the original predetermination date asset was stock titled in the husband's name and that the stock would have been marital property had it been acquired during marriage and after the determination date. The stock is therefore potentially deferred marital property subject to the wife's election under section 861.02 if she survives her husband. Is a subsequent acquisition during marriage and after the determination date that is traceable to the original asset deferred marital property subject to the wife's election under section 861.02 if she survives her husband, he dies domiciled in Wisconsin, and he still owns the asset at his death? The answer is not expressly set forth in the Act. Section 851.055, which defines deferred marital property, does not include a tracing rule and only applies to acquisitions made before chapter 766 applies. The better rule is that mere sale or exchange during marriage and after the determination date (that is, while chapter 766 applies) should not eliminate what would otherwise be an asset's deferred marital property status. Section 766.31(8) states that the reinvestment retains the classification and ownership rights of its predetermination date property source if traceable to that source, and the policy behind the deferred marital property election is a strong one. Thus, section 766.31(8) should be interpreted to mean that an asset acquired during marriage and after the determination date (that is, while chapter 766 applies) retains the deferred marital property character of the source to which it is traceable.

The tracing rule in section 766.31(8) is implicit in UMPA and the Act as originally enacted. *See* Wis. Stat. Ann. § 766.31(8) Legis. Council Notes—1985 Act 37, §§ 76 to 83 (West 2009). An asset that cannot be traced to predetermination date property is reclassified as marital property. Wis. Stat. § 766.63(1). The Act provides other means of reclassifying predetermination date property to marital property, such as a marital property agreement or, for example, an attempt by spouses under document of title to establish a joint tenancy (in which case the property becomes survivorship marital property). *See* Wis. Stat. Ann. § 766.31(8) Legis. Council Notes—1985 Act 37, §§ 76 to 83 (West 2009); *see also* Wis. Stat. § 861.02(2) (presuming property at death to be deferred marital property if presumption favorable to marital property is rebutted); *infra* §§ 2.283–.295 (reclassification methods).

An analogous case involves a spouse who acquires separate property while domiciled in a common law state, changes domicile to a community property state, sells the separate property, and reinvests the

proceeds. It has been stated that community property jurisdictions characterize the reinvestment as separate property if tracing to the source is possible. See A.M. Swarthout, Annotation, *Change of Domicil as Affecting Character of Property Previously Acquired as Separate or Community Property*, 14 A.L.R.3d 404 (1967).

## **X. Mixed Property [§ 2.155]**

Frequently, an asset's classifications will be mixed so that it is not wholly individual, marital, or predetermination date in character. Except for certain life insurance policies and deferred-employment-benefit plans, mixing marital property with property having any other classification reclassifies the other property to marital property unless the component of the mixed property that is not marital property can be traced. Wis. Stat. § 766.63(1). Consistent with the presumption that all spousal property is marital property, Wis. Stat. § 766.31(2), the party seeking to establish the nonmarital property component of a mixed asset has the burden of tracing that component. In addition, different types of predetermination date property can be mixed: property that constitutes deferred marital property can be mixed with property that does not constitute deferred marital property. See *infra* ch. 3. After a spouse's death, if it can be proved that an asset is not marital property, the burden of tracing the component that is not deferred marital property, for the purpose of separating it from the deferred marital property component, is still on the party seeking to trace the component that is not deferred marital property. See Wis. Stat. § 861.02(2). Neither the Act nor UMPA specifies tracing rules. It is contemplated that tracing rules will be developed by the case law of the adopting state. These matters are considered in chapter 3, *infra*.

## **XI. Life Insurance [§ 2.156]**

### **A. In General [§ 2.157]**

Life insurance policies and deferred employment benefits are subject to special classification rules that function independently of section 766.31. These benefits and policies are examined in sections 2.158–.183 and 2.184–.219, *infra*, respectively.

Section 766.61 of the Act, based in large part on section 12 of UMPA, classifies the ownership interest in and proceeds of all life insurance policies insuring spouses. The Act does not provide specific classification rules if section 766.61 does not apply (as it would not, for example, if a policy owned by a spouse insured a third person such as a child or business partner); presumably, the general classification rules set forth in other sections of the Act apply to such a policy.

➤ **Note.** Section 766.61 does not apply to a policy held by a deferred-employment-benefit plan. Wis. Stat. § 766.61(8). Deferred employment benefits, regardless of the nature of the assets held by the deferred-employment-benefit plan, are classified under section 766.62.

## **B. Definitions [§ 2.158]**

### **1. In General [§ 2.159]**

Of the terms defined in section 766.61, four have primary importance: policy, owner, ownership interest, and proceeds. The date a policy becomes effective and the definition of during marriage must also be considered.

### **2. Policy [§ 2.160]**

For the general purposes of section 766.61, the term *policy* means an insurance policy insuring the life of a spouse and providing for payment of death benefits at that spouse's death. Wis. Stat. § 766.61(1)(c). For purposes of section 766.61(3)(e) (dealing with written consents), however, the term policy includes an insurance policy insuring the life of any individual and providing for payment of death benefits at the insured's death. *Id.* Unless otherwise indicated in sections 2.161–.183, *infra*, the term policy means a policy as defined for the general purposes of section 766.61.

### **3. Owner [§ 2.161]**

For the purposes of section 766.61, the term *owner* means either (1) the person appearing on the policy issuer's records as having the

ownership interest or (2) the insured, if no other person appears on those records as the person having the ownership interest. Wis. Stat. § 766.61(1)(a).

In the case of group insurance, the term owner means the holder of each individual certificate of coverage under the group plan; it does not mean the person who contracted with the policy issuer on the group's behalf, whether or not the person is listed as the owner on the contract. *Id.*

The above definitions do not determine ownership as a matter of property law or classification between spouses; those rights are determined by the applicable classification rules. In regard to life insurance policies, the terms *own* and *ownership interest* have the special meanings given in subsections 766.61(1)(a) and (b), unless otherwise indicated. The owner of a policy, however, has all the rights of management and control of the policy. Wis. Stat. § 766.51(1)(d). In addition, as used in sections 2.162–.183, *infra*, the term *record owner* means an owner for purposes of section 766.61.

#### **4. Ownership Interest [§ 2.162]**

Except as provided in section 766.61(3)(e) concerning written consents, the term ownership interest means an owner's rights under a policy. Wis. Stat. § 766.61(1)(b). In connection with written consents, the term includes the interests of a spouse who is not named as an owner on the policy issuer's records. Wis. Stat. § 766.31(3)(e); *see infra* § 2.177.

#### **5. Proceeds [§ 2.163]**

The term *proceeds* means “the death benefit from a policy and all other economic benefits from it, whether they accrue or become payable as a result of the death of an insured person or upon the occurrence or nonoccurrence of another event.” Wis. Stat. § 766.61(1)(d).



## 6. Effective Date of Policy [§ 2.164]

When applying the classification rules and apportionment formulas applicable to life insurance, *see infra* §§ 2.168–.172, it is often necessary to determine both a policy’s issuance date and its effective date. The effective date is important in applying apportionment formulas in section 766.61(3), which are expressed in terms of when the policy is “in effect.” Section 766.61(2m) establishes a policy’s effective date with respect to nongroup and group policies.

For purposes of determining the marital property component of the ownership interest and proceeds of a *nongroup* policy, the policy’s effective date is the date of original issuance or the date of coverage, whichever is earlier, if the policy is thereafter kept in force merely by continuing premium payments, without any further underwriting. Wis. Stat. § 766.61(2m)(a). If additional underwriting is required after the policy’s original issuance, or if the proceeds increase after the original issuance because of unscheduled additional premiums paid by the policyholder, the policy’s effective date is the date on which the newly underwritten or newly increased coverage begins. *Id.* Questions of interpretation arise because a policy’s effective date occurs after the issuance date when additional underwriting is required or when an unscheduled premium is paid. For a discussion of these questions in connection with section 766.61(3)(a)–(d), *see* section 2.174, *infra*.

For purposes of determining the marital property component of the ownership interest and proceeds of a *group* policy, the policy’s effective date is the date individual coverage begins, even if the sponsoring employer or association subsequently changes policy issuers or the amount of coverage. Wis. Stat. § 766.61(2m)(b). Thus, classification will not change simply because an employer or association changes its policy issuer. If additional underwriting is required after the group policy’s original issuance or if coverage is provided by a different employer or association, the policy’s effective date is the date on which the newly underwritten or newly provided coverage begins. *Id.* A policy’s issuance date and effective date may not be the same. *See infra* § 2.174.

The Act does not define the term *underwriting*.

## **7. During Marriage [§ 2.165]**

The formulas developed under section 766.61 to determine a policy's marital property component often require the calculation of a numerator that among other factors refers to a period "during marriage." It must be remembered that section 766.01(8) defines the term during marriage to mean "a period in which both spouses are domiciled in this state that begins at the determination date and ends at dissolution or at the death of a spouse." Thus, a marital property component in a policy cannot accrue for any time during which the insured or the insured's spouse is not domiciled in Wisconsin, even though the spouses remain married. *See supra* § 2.8.

### **C. Classification Rules [§ 2.166]**

#### **1. In General [§ 2.167]**

Although certain interests are given special treatment in section 766.61 (e.g., interests of certain creditors, payors, recipients of support obligations, *see infra* §§ 2.179–.182), the basic classification rules for life insurance policies and their consequences are set forth in section 766.61(3). Based in large part on section 12(c) of UMPA, section 766.61(3) applies to any insurance policy on the life of a spouse, whether the policy is owned by that spouse or by the other spouse, and whether it is issued, or paid for, either before or after the determination date. Whether section 766.61(3) applies to a policy owned by a third person is considered in section 2.172, *infra*.

#### **2. Policy on Owner Spouse [§ 2.168]**

##### **a. Policy Issued During Marriage and After Determination Date [§ 2.169]**

A life insurance policy issued after the determination date designating the insured spouse as the owner is marital property, except as provided in section 766.61(3)(a)2. Wis. Stat. 766.31(3)(a)1. The ownership interest and proceeds of such a policy are marital property *regardless* of the classification of property used to pay premiums on the policy.

➤ **Example 1.** Assume that during marriage and after the determination date, a husband applies for and is the record owner of a \$100,000 insurance policy on his life and that he pays all premiums with cash he inherited. Even though payment of all premiums was from his nonmarital property, the ownership interest in the policy and its proceeds is classified as marital property. The source of premium payments is irrelevant for a policy when the insured spouse is the record owner and the policy was issued during marriage and after the determination date. Because the insurance proceeds are marital property, the husband's surviving spouse could claim \$50,000 of the proceeds if the husband designates a third person as the beneficiary without his wife's written consent or agreement. See Wis. Stat. § 766.70(6)(b)1.

Section 766.61(3)(a) does not deal with the classification of a policy or its proceeds after the dissolution of a marriage when the insured may continue to pay premiums out of his or her solely owned property. The policy may be assigned by a divorce decree. A decree's failure to mention the policy may mean that each former spouse owns, as an equal tenant in common, an undivided one-half interest in the former marital property component of the policy and in the proceeds attributable to that component. See Wis. Stat. § 766.75.

Section 766.61(3)(a)2. deals with the classification of such a policy after either or both of the spouses change domicile to another state. If a life insurance policy is issued after the determination date designating the insured spouse as the owner, and after the policy's issuance the insured or the insured's spouse is at any time not domiciled in Wisconsin, the ownership interest and proceeds of the policy become mixed property. Wis. Stat. § 766.61(3)(a)2. The marital property component of the ownership interest and proceeds is the amount that results from multiplying the entire ownership interest and proceeds by a fraction, the numerator of which is the period during marriage that the policy was in effect, see *supra* § 2.165, and the denominator of which is the entire period that the policy was in effect. Wis. Stat. § 766.61(3)(a)2.

➤ **Example 2.** Assume that a policy is issued after the determination date to the insured spouse who is the record owner. The policy is in effect for 15 years, and the insured and the insured's spouse are married the entire time. At the beginning of the 10th year, the insured's spouse changes domicile from Wisconsin to a common law

state. Based on these facts, two-thirds of the entire ownership interest and proceeds of the policy is marital property. The other one-third is nonmarital property.

➤ **Note.** Section 766.61(3)(a)2. became part of the Act as the result of the 1988 Trailer Bill and does not affect rights that accrued before May 3, 1988, the effective date of the 1988 Trailer Bill. Wis. Stat. § 766.03(5). Thus, section 766.61(3)(a)2. should not deal with policies issued after the determination date when the insured's spouse was named as a record owner before May 3, 1988, and the insured or his or her spouse was domiciled outside Wisconsin after the determination date but before May 3, 1988.

For a discussion of the relationship between section 766.61(2m)(a) (dealing with additional underwriting or payment of unscheduled premiums) and section 766.61(3)(a), see section 2.174, *infra*. As to the impact of the deferred marital property rules on life insurance policies and proceeds, see sections 2.242 and 12.148, *infra*.

### **b. Policy Issued Before Determination Date with Premiums Paid After That Date [§ 2.170]**

Section 766.61(3)(b) deals with life insurance policies issued before the determination date and designating the insured spouse as the owner. If a policy is issued before the determination date designating the insured spouse as the owner, and all premiums paid after the determination date are paid from nonmarital property, the policy and proceeds remain nonmarital property; however, all or a portion of the policy may be subject to the deferred marital property election. *See infra* § 2.242.

If, however, even one premium on such a policy is paid from marital property funds after the determination date, the policy becomes a type of mixed property. After a premium is first paid from marital property funds, the source of future premium payments is irrelevant; the marital property component of the ownership interest and proceeds of the policy is determined by a formula based, in large part, on the time before and after a premium is first paid from marital property funds. The marital property component is the amount that results from multiplying the entire ownership interest and proceeds by a fraction, the numerator of which is the period during marriage that the policy was in effect after the date on

which a premium was first paid from marital property funds, and the denominator of which is the entire period that the policy was in effect. Wis. Stat. § 766.61(3)(b); *see supra* § 2.165 (statutory definition of during marriage). Thus, either the inadvertent or the deliberate payment of only one premium from marital property funds creates a marital property component that grows over time.

➤ **Comment.** Section 766.61(3)(b) refers to the date when “a premium” is first paid from marital property after the determination date. A question arises whether the time apportionment formula is triggered if only a *portion* of a premium is paid from marital property funds and the balance from nonmarital property funds. It is difficult to imagine what the outcome would be if the words a premium do not include a portion of a premium. Perhaps some system of reimbursement could be devised, but it appears that the intent of section 766.61(3)(b) is to establish as simple a rule as possible. In keeping with that intent, it appears that the words “a premium” should be read to mean, in effect, “a premium or portion of a premium.”

➤ **Example 1.** Assume that a policy is issued before the determination date designating the insured spouse as the owner. The policy is in effect for 15 years, and the insured and his or her spouse are married the entire time. A premium is first paid from marital property funds after the determination date at the beginning of the 10th year; premiums for the next 5 years are paid from nonmarital property funds. Based on these facts, one-third of the entire ownership interest and proceeds of the policy is marital property. After one premium is paid from marital property funds, the source of subsequent premium payments is irrelevant. The balance of the proceeds is nonmarital property, some of which may be deferred marital property. *See infra* § 2.242.

Section 766.61(3)(b) does not expressly tell how to adjust the apportionment formula if the insured or his or her spouse is no longer domiciled in Wisconsin. Section 2.169, *supra*, explains that such adjusting language is used in connection with life insurance policies issued to a spouse after the determination date. No adjusting language is necessary in connection with section 766.61(3)(b) because the definition of the term during marriage in section 766.01(8) when read in combination with the time-apportionment formula provided in section 766.61(3)(b) automatically apportions marital property interests and

nonmarital property interests if one or both of the spouses are no longer domiciled in Wisconsin. *See* Wis. Stat. Ann. § 766.61(3)(c)2. Legis. Council Committee Notes—1987 Act 393 (West 2009).

➤ **Example 2.** Assume the same facts as in Example 1 above, but assume that either the insured or his or her spouse changes domicile to another state on the final day of the 11th year after the policy was issued and that he or she remains domiciled outside Wisconsin. In that case, only 1/15th of the entire ownership interest and proceeds of the policy is marital property.

Upon the dissolution of a marriage, the marital property component of a policy subject to section 766.61(3)(b) ceases to grow because the numerator of the fraction refers to the period during marriage, which ends at dissolution. As to the effect of a divorce decree, see section 2.169, *supra*.

For a discussion of the consequences of additional underwriting or payment of unscheduled premiums in connection with a policy issued before the determination date, see section 2.174, *infra*.

### **3. Policy on Spouse Designating Other Spouse as Owner [§ 2.171]**

If the insured's spouse is the record owner of the life insurance policy, then the ownership interest and proceeds of the policy are the individual property of the record owner spouse, except as provided in section 766.61(3)(c)2. Wis. Stat. § 766.61(3)(c)1. The ownership interest and proceeds remain the individual property of the record owner spouse, regardless of the classification of property used to pay premiums on the policy. *Id.* Section 766.61(3)(c) makes no distinction between policies issued before and after the determination date. Neither does section 766.61(3)(c) distinguish between a policy designating the noninsured spouse as owner from issuance and a policy first issued to the insured spouse who later transfers it to the noninsured spouse.

Because a policy described in this section is the individual property of the record owner spouse, it follows that amounts borrowed from such a policy are also that spouse's individual property. It is not clear, however, what classification attaches to the dividends on such a policy when such

dividends exceed aggregate premiums paid. Such excess dividends are considered income under section 766.01(10), and the general rule is that income from individual property is marital property. Wis. Stat. § 766.31(4). However, if the policy is a spouse's individual property because a gift was made of the policy by the insured spouse to the noninsured spouse, the income is individual property unless a contrary intent of the insured spouse regarding the income's classification is established. Wis. Stat. § 766.31(10).

After the issuance of a policy designating the noninsured spouse as the owner, if either the insured or his or her spouse is at any time not domiciled in Wisconsin, a portion of the ownership interest and proceeds of the policy is individual property, and a portion is other than individual or marital property. Wis. Stat. § 766.61(3)(c)2. The individual property component of the ownership interest and proceeds is the amount that results from multiplying the entire ownership interest and proceeds by a fraction, the numerator of which is the entire period during which the policy was in effect, less that period during which the insured or his or her spouse was at any time not domiciled in this state, and the denominator of which is the entire period that the policy was in effect. *Id.* Thus, the operative period for determining the individual property component is the period during which both spouses are domiciled in Wisconsin after the policy is issued. The portion of the policy that is not individual property cannot be marital property; presumably, that portion may be classified under the laws of the state in which the record owner is domiciled.

As to the relationship between section 766.61(2m)(a), governing a policy's effective date, and section 766.61(3)(c), see section 2.174, *infra*.

#### **4. Policy on Spouse Owned by Third Party [§ 2.172]**

Section 766.61(3)(d) applies to a life insurance policy insuring a spouse and designating a person other than either spouse as the policy's owner. If no premiums are paid from the spouses' marital property funds, the ownership interest and proceeds are unaffected by chapter 766. Wis. Stat. § 766.61(3)(d), (6). But if at least one premium is paid from the spouses' marital property funds, the ownership interest and proceeds of the policy are in part property of the designated policy owner and in part the spouses' marital property, regardless of the classification of property used to pay premiums after the initial payment of a premium

from marital property. The mathematical formula used to determine the marital property component of the ownership interest and proceeds is the same as that set forth in section 766.61(3)(b). *See supra* § 2.170. Thus, the marital property component of the ownership interest and proceeds is the amount that results from multiplying the entire ownership interest and proceeds by a fraction, the numerator of which is the period during marriage that the policy was in effect after the date on which a premium was first paid from marital property funds, and the denominator of which is the entire period the policy was in effect. Wis. Stat. § 766.61(3)(d); *see supra* § 2.165 (statutory definition of during marriage).

➤ **Note.** Another view is that the premiums paid from the spouses' marital property funds are a completed gift with the result that section 766.61(3)(d) would not apply. This point is discussed later in this section.

If section 766.61(3)(d) applies, its time-apportionment formula must be adjusted if one or both of the spouses from whose marital property a premium was paid are no longer domiciled in Wisconsin. The definition of the term during marriage when read with the time-apportionment formula in section 766.61(3)(d) automatically apportions the marital property and nonmarital property interests if one or both of the spouses are no longer domiciled in Wisconsin. *See supra* § 2.170.

A typical business-based life insurance policy (e.g., a “key-employee” policy owned by a corporation) is an example of a policy owned by a third party but insuring a spouse. Ordinarily, no portion of the policy is marital property because the business owns the policy and pays the premiums. UMPA § 12 cmt. (The same result obtains if another partner or stockholder owns the policy and pays the premiums.)

If an entire policy insuring a spouse (including one subject to a split-dollar arrangement) is owned by a third party, then from the date a premium is first paid from marital property of the insured and his or her spouse, the policy and proceeds have a marital property component subject to the formula set forth in section 766.61(3)(d).

➤ **Example 2.** Suppose that an adult child owns a policy insuring his father and the father pays a premium from marital property directly to the insurance company. In such a case, a marital property



component is created. *See* Wis. Stat. § 766.61(3)(d). The child owns the balance.

Some may argue that payment of the premium in the above example is a gift to the child (subject to remedies of the father's spouse in section 766.70 if the premium paid exceeds the dollar amounts of section 766.53) and that a completed gift to a third person can no longer be marital property. If that is true, however, it is difficult to conceive of a situation in which a marital property component would be created under section 766.61(3)(d).

On the other hand, a case can be imagined in which application of section 766.61(3)(d) leads to incongruous results. Assume that in Example 2 above the father paid the very first premium from marital property funds and the child then paid all subsequent premiums from marital property funds owned by the child and his or her spouse. Under a literal application of section 766.61(3)(d), the time-apportionment formula producing the marital property component owned by the child's parents would begin on the date the first premium was paid from the parents' marital property funds. However, the child also used marital property funds to pay premiums. Under these circumstances, would the child, the child's spouse, and the child's parents have overlapping marital property interests in the policy and proceeds? The Act does not provide an answer.

Suppose, though, that the father in Example 2 made a completed gift of marital property cash to his child and that all marital property interests in the gift were reclassified and divested—perhaps because the father's spouse acted together with the father in the gift or simply because such a gift is complete from the moment of transfer (although if the gift exceeded the dollar amounts of section 766.53, it would be subject to the other spouse's remedies under section 766.70(6)(a)). Suppose also that the child then paid the premium from the funds acquired by gift or from his or her other assets. Under these circumstances, a marital property component with respect to the father's marriage should not be created under section 766.61(3)(d), assuming that the child was not acting as the father's agent, because the cash was no longer marital property.

A policy insuring a spouse may be owned by an irrevocable insurance trust entirely for a third party's benefit. If the insured spouse uses marital property to pay the premiums directly to the insurance company, a marital property component may be created under section 766.61(3)(d).

The same result may obtain if a business under a noncontributing split-dollar arrangement pays premiums directly to the insurance company because that portion based on PS 58 or PS 38 costs is treated as compensation of the insured spouse. (PS 58 and PS 38 refer to the economic benefit received by the employee by way of insurance protection, using government premium rates. See, for example, I.R.S. Notice 2002-8, 2002-4 I.R.B. 398.)

What if marital property cash is transferred to the trust and the trustee pays the premium? Will a marital property component exist under section 766.61(3)(d), or is this case similar to the example in the preceding paragraph, in which a transfer of cash was made to an adult child who then paid the premium? In such circumstances, section 766.31(5) may play a role.

Section 766.31(5) provides that a transfer of property to a trust does not by itself change the classification of the property so transferred. It is believed that if the trust is irrevocable, the fact of irrevocability suffices to make the transfer a completed gift and thereby reclassify the property. See *supra* §§ 2.98–104. In these circumstances, section 766.61(3)(d) should not apply. If the transfer is unilaterally accomplished by a spouse with management and control, it should be a completed gift, subject to the other spouse's remedies, including that under section 766.70(6)(a). See *id.*; see also *infra* ch. 10. There should be no marital property component under section 766.61(3)(d).

➤ **Practice Tip.** The cautious attorney may desire to reclassify the cash or income used to pay premiums as the settlor spouse's individual property before transferring the cash or income to the trust. Reclassification may be accomplished by gift, written consent, marital property agreement, or, in an appropriate case, unilateral statement. If the insurance trust provides an income interest for the noninsured spouse's benefit with the remainder to a third person, some of the discussion in sections 2.98–104, *supra*, may be relevant ("Marital Property Transferred to Trust by Spouse or Spouses"). In general, it is good practice to avoid using marital property to fund such a trust or to pay premiums on a policy owned by such a trust. For a discussion of tax consequences, see chapters 9 and 10, *infra*.

For a discussion of the consequences of additional underwriting or payment of unscheduled premiums in connection with a policy issued before the determination date, see section 2.174, *infra*.

## 5. Policy Insuring Third Party [§ 2.173]

The classification of a policy owned by a spouse that insures a third party is governed by classification rules in the Act other than those found in section 766.61. An example is a policy used to fund a cross-purchase arrangement. *See infra* §§ 4.79, ch. 10. Section 766.61(3)(d) may apply to such a policy if the third-party insured is married and marital property of the insured rather than property of the owner is used to pay a premium. *See supra* § 2.172.

## 6. Effect of Section 766.61(2m) on Time-apportionment Formulas [§ 2.174]

Questions may arise in connection with the relationship between section 766.61(2m)(a), governing a policy's effective date, and the time-apportionment formulas in section 766.61(3)(a), (b), (c), and (d).

➤ **Example.** Assume that a policy designating the insured spouse as owner is issued before the determination date and that after the determination date all scheduled premiums are paid with individual property. Assume that after the determination date an unscheduled premium is paid to secure additional proceeds. Does classification depend on whether the unscheduled premium is paid from marital property funds or from nonmarital property funds?

In the example, the policy was issued before the determination date, but the increased coverage began after the determination date. Under section 766.61(2m)(a), the policy has a new effective date when the right to increased proceeds begins. Does this mean the policy's issuance date can be ignored? The answer is not clear, and in certain cases, it may have significant consequences. The language of section 766.61(2m)(a) and the formulas in section 766.61(3) support the view that the two dates are not necessarily the same. Although section 766.61(2m)(a) is the only place in section 766.61 that the words *effective date* appear, the formulas in section 766.61(3) refer to when a policy is "in effect." Presumably, the words "effective date" tie to "in effect" rather than "date of issuance." In addition, section 766.61(2m)(a) states that the effective date of a nongroup policy is the date on which the newly underwritten right to proceeds or the right to increased proceeds begins, but as section 766.61(2m)(a) acknowledges, either or both of those events occur "after

original issuance of the policy.” On the other hand, it may be argued that section 766.61(2m)(a) creates a device designed to reclassify life insurance policies to marital property if additional underwriting occurs or unscheduled premiums are paid after the determination date, and to achieve that objective in full, the policy’s issuance date should be moved to its new effective date.

Consider the possible application of section 766.61(3)(a) to the above example. Section 766.61(3)(a) states that a policy issued after the determination date designating the insured spouse as owner is marital property regardless of the source of the premiums paid. If the date of issuance in the example is deemed to move up in time to the new effective date, then it is as if a new policy was issued after the determination date with the insured spouse as record owner. Such a policy is entirely marital property. If the two dates are not the same (that is, the issuance date is not moved up in time but remains as is), then section 766.61(3)(a) is inapplicable because the policy in the example was not issued after the determination date.

Assuming, in the example, that the issuance date and the effective date cannot be read to be the same, the application of section 766.61(3)(b) must be considered. If a policy issued before the determination date designates the insured as the owner, the policy and its proceeds become mixed property if a premium is paid from marital property funds after the determination date. A formula is established to determine the marital property component. The marital property component is the amount that results from multiplying the entire ownership interest and proceeds by a fraction, the numerator of which is the period during marriage that the policy was in effect after the date on which a premium was first paid from marital property funds, and the denominator of which is the entire period that the policy was in effect. *See supra* § 2.165 (statutory definition of during marriage).

When no additional proceeds are purchased, the time-apportionment formula is clearly understood. In the example, however, an additional unscheduled premium was paid. That automatically gave the policy an effective date after the determination date. If the unscheduled premium was paid from marital property funds, it appears that the entire policy is reclassified as marital property because the numerator and the denominator in the formula set forth in section 766.61(3)(b) are the same.

What if nonmarital property funds were used to pay the unscheduled premium? The time-apportionment formula in section 766.61(3)(b) computes a marital property component only after a premium is paid from marital property funds. If only nonmarital property funds were used to pay premiums, the fact that the policy has a new effective date seems to be irrelevant. Note, however, that even though the policy may not be reclassified as marital property, there are still property law consequences (assuming the issuance date is not moved up to the new effective date). A new effective date alters the formula. Thus, if a premium is subsequently paid from marital property funds, the denominator begins on the policy's new effective date, so that time elapsed between the issuance date and the new effective date is ignored, thereby enlarging the marital property component.

The formula in section 766.61(3)(d), involving policies owned by a third party, is the same as that in section 766.61(3)(b). Thus, the foregoing discussion should be relevant to section 766.61(3)(d). The foregoing discussion may be moot as far as section 766.61(3)(c) is concerned because a policy owned by a spouse insuring the life of the other spouse is the owner spouse's individual property regardless of the source of the premiums.

#### **D. Deferred Marital Property [§ 2.175]**

For application of the deferred marital property rules to life insurance policies and proceeds, see sections 2.242 and 12.136, *infra*.

#### **E. Comparison with Other Community Property States [§ 2.176]**

The Wisconsin classification system used for life insurance policies subject to section 766.61 is quite different from the systems found in other community property jurisdictions. Some community property jurisdictions use rules based on inception of title or source of premiums. Under the rule based on inception of title (used in Texas, for example), marital status when the first premium is paid determines the ownership of the policy. *See* McClanahan, *supra* § 2.4, at 363. If subsequent premiums are paid from property of another classification, a claim for reimbursement usually arises to the extent of the amount of premiums paid, rather than as a pro rata proportion of the proceeds when paid. The

rule based on source of premiums (used in California, for example), is different. *Id.* Ownership of the policy and the proceeds is apportioned according to the amount of premiums paid from separate property and community property. *See also* Reppy & Samuel, *supra* § 2.19, at 88 (“Elsewhere the last premium is viewed as the sole source of the proceeds payable at the insured’s death—earlier payments are viewed as buying coverage for a period that has expired.”) (citing cases from Idaho, New Mexico, and Arizona).

Wisconsin, on the other hand, uses UMPA’s rule that a policy is entirely marital property if it is issued after the determination date and is owned by the insured spouse. In other cases in which the insured is a spouse, Wisconsin applies UMPA’s time-apportionment formula. *See* UMPA § 12; *see also supra* § 2.170. Consequently, rules from other community property jurisdictions will be of limited value when classifying life insurance policies insuring spouses domiciled in Wisconsin.

➤ **Note.** Classification of a policy owned by a spouse and insuring a third party is not governed by section 766.61. *See supra* § 2.173. Presumably, the policy must be classified under the Act’s general classification rules, and in these cases, precedent from other community property jurisdictions may be relevant.

## F. Written Consent [§ 2.177]

A written consent is a document signed by a person against whose interests it is sought to be enforced. Wis. Stat. § 766.01(16). Consents can be useful for policies that insure a settlor spouse and are held by an irrevocable insurance trust naming the other spouse as a trust beneficiary. *See infra* ch. 10. A consent is also useful for a policy owned by an insured spouse who wishes to name a beneficiary other than the other spouse.

Section 766.61(3)(e) reads in part as follows:

A written consent in which a spouse consents to the designation of another person as the beneficiary of the proceeds of a policy or consents to the use of property to pay premiums on a policy is effective, to the extent that the written consent provides, to relinquish or reclassify all or a portion of that spouse’s interest in property used to pay premiums on the policy or in the

ownership interest or proceeds of the policy without regard to the classification of property used by a spouse or another person to pay premiums on that policy. Unless the written consent expressly provides otherwise, a written consent under this paragraph is revocable in writing and is effective only with respect to the beneficiary named in it. Unless the written consent expressly provides otherwise, a revocation of a written consent is effective no earlier than the date on which it is signed by the revoking spouse and does not operate to reclassify any property which was reclassified or in which the revoking spouse relinquished an interest from the date of the consent to the date of revocation.

Note that section 766.61(3)(e) differs in many respects from section 12(c)(5) of UMPA.

Under section 766.61(3)(e), the spouse who is the record owner may designate a beneficiary. The other spouse need not participate in the actual designation, but that spouse may in writing subsequently consent to the record owner's designation and future designations.

Section 766.61(3)(e) states that the consent is revocable unless expressly provided otherwise. From a planning standpoint, irrevocable consents have the advantage of certainty. The introductory phrase in the second sentence also indicates that a written consent may specify the effect of changing a beneficiary after the written consent is executed; if the written consent is not specific on this point, the consent applies only to the beneficiary originally named in the consent.

Section 766.61(3)(e) authorizes consents purporting to deal with assets used to pay premiums. Consequently, a written consent so stating may relinquish or reclassify the consenting spouse's interest in any assets used to pay premiums. *See infra* ch. 10.

Section 766.61(3)(e) uses the important words "to the extent the consent provides." Thus, a consent to a beneficiary may relinquish or reclassify all or a portion of a consenting spouse's interest in the ownership interest and proceeds of a policy, or it could be limited to classification of property used to pay premiums (although most consents will deal with all aspects of a policy, including ownership, naming of beneficiary, and property used to pay premiums). Wis. Stat. § 766.31(3)(e).

➤ **Example.** Assume that a wife names her son as the beneficiary of a life insurance policy insuring her life and designating her as owner,

and that her husband consents in an irrevocable written consent. The consent can provide that the husband relinquishes his rights not only to the proceeds when his wife dies, but also to all other ownership interests in the policy and proceeds, without regard to the classification of property used by his wife or another person to pay premiums. A relinquishment of all ownership rights means that the wife can borrow against the policy's cash surrender value, if any, and that the proceeds of the loan are her individual property. The husband's irrevocable consent could also state that the policy, and the assets used to pay premiums as well, are reclassified as the wife's individual property despite subsequent premium payments from property of other classifications. For a discussion of tax consequences, see chapter 9, *infra*; for planning, see chapter 10, *infra*.

➤ **Comment.** Section 766.61(3)(e) as amended is a great deal more flexible than its predecessor; it specifically states that relinquishment or reclassification of a spouse's interest in property used to pay premiums or in the ownership interest or proceeds of the policy is determined according to the terms of the written consent. Consents, therefore, can be tailor-made.

Because a consent may reclassify an insurance policy described in section 766.61, it should be possible to reclassify a predetermination date policy (even one with a component potentially subject to the deferred marital property election) as the individual property of the insured spouse.

Unless it is expressly irrevocable, a consent may be revoked. Unless the written consent provides otherwise, a revocation is effective no earlier than the date it is signed by the revoking spouse. Any implication that a revocation may be retroactive is inconsistent with the general rule that a spouse may not unilaterally reclassify the other spouse's property interests. Thus, unless the written consent itself so provides, a revocation of the consent does not reclassify any property that was reclassified by the written consent or any property in which the revoking spouse relinquished an interest during the period between the date of consent and the date of revocation. Wis. Stat. § 766.61(3)(e). After a revocation, the ownership rules and formulas under section 766.61 begin to apply. For a discussion of the tax and planning consequences of revocation, see chapter 10, *infra*.



➤ **Caveat.** There may be uncertainty about whether a written consent can apply to insurance policies acquired after the written consent is executed. Section 766.61(3)(e) refers to “a policy,” perhaps implying that the policy must be in existence or applied for at the date of the consent. The better rule permits a consent to apply to after-acquired policies and substituted policies. A marital property agreement can apply to after-acquired property. Wis. Stat. § 766.58(3)(a); *see infra* ch. 7.

## G. Spousal Remedies [§ 2.178]

If a spouse with management and control unilaterally transfers a life insurance policy that is marital property to a third person or entity, whether the nondonor spouse may invoke remedies under section 766.70(6)(a) turns on whether the gift’s value is within the dollar amounts of section 766.53. Section 766.53 has special rules dealing with gifts of life insurance policies. For a discussion of life insurance policies and available remedies, see sections 8.50–.52, *infra*. For a discussion of tax consequences, see section 9.51, *infra*. For a discussion of elective rights in connection with deferred marital property life insurance policies, see sections 2.242 and 12.151, *infra*.

Sections 766.70(7) and 766.61(7) deal with the rights of the spouses when the noninsured spouse dies first.

➤ **Example.** Assume that a husband purchases and is record owner of a \$200,000 policy on his life after the determination date. The policy is classified as marital property. *See supra* § 2.169. The policy’s interpolated terminal reserve and unused portion of the term premium is \$10,000 when the husband’s wife predeceases him. What interest does the wife’s estate have in the policy on the surviving husband’s life?

In the example, the wife’s interest in the policy at the time of her death is \$5,000. Under section 766.70(7), a surviving spouse may purchase the deceased spouse’s interest in the policy from the deceased spouse’s estate within the time limitations set forth in that section. What if the purchase is not made? The surviving husband continues to own at least half the policy. What about the interest of the wife’s estate?

Section 766.61(7) provides that the interest of the wife's estate is limited to a dollar amount equal to one half the marital property interest in the interpolated terminal reserve and in the unused portion of the term premium of the policy on the date of her death (in the example, \$5,000). All other rights of the decedent wife in the ownership interest and proceeds of the policy terminate. All other rights are owned by the husband. See section 12.13, *infra*, for a more detailed discussion.

An exception to the application of section 766.61(7) is provided in section 854.14(3m)(b)2., which applies when the predeceasing spouse is murdered by the insured spouse. In such a case, the decedent's interest is a fractional interest equal to one-half the portion of the policy that was marital property immediately before the death of the decedent spouse. Thus, if the policy had a cash surrender value of \$100,000 on a policy paying a death benefit of one million dollars, then the decedent spouse's interest is a fractional interest equal to one-half the cash surrender value. Because the statute is expressed in terms of a fractional interest (not dollar terms) and, according to the Committee Notes, is not frozen, the implication is that the decedent spouse's estate plan passes a one-half ownership interest in the policy to the decedent spouse's nonspousal beneficiaries. Presumably those beneficiaries have an obligation to pay half of all future premiums.

## **H. Protected Parties [§ 2.179]**

### **1. Payors [§ 2.180]**

The general rule is that a policy issuer may rely on and act in accordance with the policy and the issuer's records and that if the policy issuer makes payments or takes actions in accordance with the policy and the issuer's records, the issuer is not liable because of those payments or actions. Wis. Stat. § 766.61(2)(b)1. Accordingly, the classification of a policy or a portion of a policy as marital property has no effect on the policy issuer's duty to perform under its contract when making payment or taking action in accordance with the policy and its records. Wis. Stat. § 766.61(2)(b)2.

A major exception to the rule occurs if at least five business days before making payment or taking action in accordance with the policy and the issuer's records, a policy issuer receives at its home office a notice of claim. Wis. Stat. § 766.61(2)(c)1. A notice of claim means a

written notice, by or on behalf of a spouse, former spouse, surviving spouse, or person claiming under a deceased spouse's disposition at death, that the person sending the notice claims to be entitled to the proceeds, the payments, or an interest in the policy. Wis. Stat. § 766.61(2)(a)2.

Upon receipt of a notice of claim, the issuer must notify the party directing the payment or action (usually a person claiming to be a beneficiary) that a notice of claim has been received. The issuer may not take any action on the policy for 14 business days after receiving the notice of claim. Wis. Stat. § 766.61(2)(c)1.

Within 14 business days after receiving the notice of claim the issuer must receive at its home office, as purporting to support the notice of claim, a decree, marital property agreement, written directive signed by the beneficiary and surviving spouse, consent under section 766.61(3)(e), or proof that a legal action has been filed, including a copy of an election filed under section 861.08 (deferred marital property election), to secure an interest as evidenced in such a document. If appropriate documentation in support of the claim is received on a timely basis, the issuer may make payment or take action on the policy only after the issuer receives documentation from a court, or from the claimant and the person directing action or payment, indicating that the dispute has been resolved. Wis. Stat. § 766.61(2)(c)2. (Presumably, other forms of appropriate documentation should also suffice.)

If documentation purporting to support the claim is not submitted as and within the time limits described, the policy issuer "shall" take action or make payment as if there had been no notice of claim in the first place. Wis. Stat. § 766.61(2)(c)3. A policy issuer is not liable to any person for any claim for damages as a result of the suspension of policy action or the taking of any action under section 766.61(2). Wis. Stat. § 766.61(2)(d). However, a policy issuer must pay interest that accrues during the suspension of any action. *Id.*

➤ **Note.** Section 766.61(2)(c) does not define the term *policy issuer*. Consequently, questions may arise whether payors under self-insured plans are policy issuers within the meaning of section 766.61(2). If they are not policy issuers under that section, they might not enjoy the protection that section affords.

## 2. Creditors [§ 2.181]

Section 766.61(4), based on section 12(d) of UMPA, states that section 766.61 does not affect a creditor's interest in the ownership interest or proceeds of a policy that is assigned to the creditor as security or made payable to the creditor.

## 3. Owners or Beneficiaries of Policies Subject to Certain Decrees and Property Settlements [§ 2.182]

Section 766.61(5), based on section 12(e) of UMPA, states that the interest of a person as owner or beneficiary of a policy acquired under a decree or property settlement agreement incident to a prior marriage or to parenthood is not marital property, regardless of the classification of property used to pay the premiums.

➤ *Example.* Suppose that a divorce decree names a husband as owner of an insurance policy on his life and requires him to maintain the policy for the benefit of his child from a prior marriage. Such a policy is the husband's nonmarital property, and the implication is that the proceeds could be paid free of any claims by the husband's second spouse, even if marital property funds were used to pay the premiums. Perhaps a claim for reimbursement from the husband could be made for marital property funds used to pay the premiums.

### I. Policy Dividends [§ 2.183]

Certain life insurance policies permit the use of dividends either to purchase additional insurance or to reduce premium payments.

➤ *Example.* Assume that a wife owns an insurance policy on her life and that the policy is her individual property. The aggregate policy dividends earned or accrued during marriage and after the determination date are not income until they exceed aggregate premiums paid. Wis. Stat. § 766.01(10); *see supra* § 2.165 (statutory definition of during marriage). Once dividends constitute income earned or accrued during marriage and after the determination date, they are marital property (assuming no interspousal gift and no

marital property agreement, court decree, written consent, or unilateral statement to the contrary), and using such income to pay premiums results in a mixed asset under section 766.61(3)(b). (Mixing under section 766.63(1) would occur if the policy owned by the wife insured a third person.)

What if the wife in the above example uses the dividends to purchase additional insurance? Whether the policy dividends constitute income does not depend on what the dividends are used for but rather on whether the aggregate dividends exceed the aggregate premiums paid. Wis. Stat. § 766.01(10). Following this line of reasoning, dividends used to pay for additional insurance are not income until the aggregate dividends exceed the aggregate premiums paid. *Id.* But this does not fully answer the question.

Even if the dividends are not income, the issue is whether each addition to the policy should be treated as the purchase of a new and separate policy. If an addition is treated as a new policy, that new policy might be marital property. For example, any policy insuring a spouse that is owned by that spouse and issued after the determination date is marital property regardless of the classification or source of premiums paid. Wis. Stat. § 766.61(3)(a); *see supra* § 2.169. It appears, however, that each paid-up addition is an adjustment as an incident to an existing contract; the addition is not a new policy because the addition is not being offered as a new and independent contract to a customer, it does not involve a test of insurability, and it is not a payment of an unscheduled premium. *See supra* § 2.164.

What if the wife borrows from her individual property policy and later repays the loan with dividends? Income does not exist until the aggregate dividends exceed the aggregate premiums paid; only at this point may mixing occur. Without an interspousal gift, a unilateral statement, or a marital property agreement or court decree to the contrary, dividends earned or accrued during marriage and after the determination date in excess of the aggregate premiums paid are marital property. If the loan is repaid with marital property, a mixing problem may arise. *Cf. infra* §§ 3.39–41 (mixing problems resulting from use of marital property to repay loan on individual property).

## **XII. Deferred Employment Benefits [§ 2.184]**

### **A. In General [§ 2.185]**

Deferred employment benefits are benefits from a deferred-employment-benefit plan. Wis. Stat. § 766.01(3m). Deferred-employment-benefit plans, in turn, are generally plans providing some form of deferred compensation. Wis. Stat. § 766.01(4). Although deferred employment benefits are a form of income for purposes of the Act, Wis. Stat. § 766.01(10), they receive distinct and special treatment under the Act. Sections 2.186–.219, *infra*, consider the definition of deferred-employment-benefit plans under the Act, the classification of deferred employment benefits, the terminable-interest rule, property and valuation issues, and administrative matters.

The impact of some of the classification rules set forth in the following sections is somewhat limited in the case of deferred-employment-benefit plans governed by the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. §§ 1001–1461. *See infra* §§ 2.214–.217.

### **B. Definition of Deferred-employment-benefit Plan [§ 2.186]**

#### **1. Statutory Definition [§ 2.187]**

Section 766.01(4)(a), based on section 1(4) of UMPA, defines the term *deferred employment benefit plan* as “a plan, fund, program or other arrangement under which compensation or benefits from employment are expressly, or as a result of surrounding circumstances, deferred to a later date or the happening of a future event.” This definition is drawn from (but is much broader than) the definition in ERISA and is intended to cover plans of both private and public employers. *See* UMPA § 1(4) cmt. The definition includes all types of deferred compensation arrangements, those that are qualified under ERISA and those that are not. *See infra* § 2.189 (list of included plans). In addition, certain plans are included in the definition in a roundabout way because of exceptions to exclusions from the definition under the Act. *See infra* § 2.191. Federal preemption may be relevant. *See infra* §§ 2.211–.217.

Deferred employment benefits are a form of income under the Act. Wis. Stat. § 766.01(10).

## **2. Significance of Definition [§ 2.188]**

What the Act includes and excludes in its definition of deferred-employment-benefit plan is significant. Only deferred compensation plans included within the definition are subject to the classification provisions of section 766.62, *see infra* §§ 2.196–.199; excluded plans are subject to the Act’s other classification provisions. Excluded plans are also not subject to the terminable-interest rule. *See infra* § 2.201. In other words, 50% of the marital property interest in an excluded plan is subject to the nonemployee spouse’s right of testamentary disposition, whereas a plan included in the definition is not subject to that testamentary disposition. *See id.*

## **3. What Definition Expressly Includes [§ 2.189]**

For purposes of the Act, deferred-employment-benefit plans include but are not limited to:

1. Pension, profit-sharing, and stock-bonus plans;
2. Employee stock-ownership or stock-purchase plans;
3. Savings or thrift plans;
4. Annuity plans;
5. Qualified bond-purchase plans;
6. Self-employed retirement plans;
7. Simplified employee pensions; and
8. Deferred compensation agreements or plans.

Wis. Stat. § 766.01(4)(a).

#### 4. What Definition Expressly Excludes [§ 2.190]

Section 766.01(4)(b), based on the last sentence of section 1(4) of UMPA, specifically excludes certain plans from the basic definition of deferred-employment-benefit plan. Subject to exceptions, *see infra* § 2.191, section 766.01(4)(b) expressly excludes “life, health, accident or other insurance or a plan, fund, program or other arrangement providing benefits similar to insurance benefits.”

➤ **Note.** Section 766.01(4)(b) does not exclude a deferred-employment-benefit plan from the basic definition simply because the plan holds life insurance policies along with other assets. Moreover, section 766.01(4)(b) does not exclude the life insurance policies held in the plan from the definition of deferred-employment-benefit plans. Regarding the classification of such life insurance policies, *see* section 2.199, *infra*.

#### 5. What Definition Includes by Exception to Exclusions [§ 2.191]

Section 766.01(4)(b) lists four exceptions (also found in section 1(4) of UMPA) to the exclusion of certain benefits from the basic definition of deferred-employment-benefit plans, thus putting these benefits back into the basic definition. Those exceptions are:

1. *Benefits having a present value immediately realizable in cash at the employee's option.* Wis. Stat. § 766.01(4)(b)1. An example is a cafeteria plan that gives an employee the option to take cash or to allocate it under various programs provided by the employer to the “purchase” of health insurance, life insurance, a pension, and so forth. Life insurance held by such a plan is subject to the deferred-employment-benefit rules under section 766.62 as opposed to the rules applying to life insurance policies under section 766.61.
2. *Benefits constituting an unearned premium for the coverage (i.e., a return of premium), to the extent of the returned amount allocable to the participant.* Wis. Stat. § 766.01(4)(b)2.
3. *Benefits representing a right to compensation for loss of income during disability.* Wis. Stat. § 766.01(4)(b)3.; *see also supra* § 2.136



(when plan in connection with such benefits commences). Because of this exception, disability benefits offered by a plan are treated as deferred employment benefits subject to the classification rules of section 766.62. Disability payments made pursuant to individually purchased disability insurance are treated differently. *See supra* § 2.136.

4. *Benefits representing a right to payment of expenses incurred before the time of valuation.* Wis. Stat. § 766.01(4)(b)4. It is not clear what is meant by the word *valuation*. Probably it means the date when classification becomes relevant. Suppose, for example, a husband incurs medical expenses, and before his plan reimburses him, his wife dies. The reimbursement the husband receives after his wife's death is apparently his solely owned property because his wife's interest in it terminated at her death. *See infra* § 2.201.

## **6. Arrangements Not Addressed by Definition [§ 2.192]**

### **a. Unfunded Plans Created Pursuant to Contracts or Partnership Agreements [§ 2.193]**

The definition of deferred-employment-benefit plan in section 766.01(4)(a) does not refer specifically to unfunded plans created pursuant to contracts or partnership agreements and paying some defined amount after retirement. Nevertheless, such plans should be included in the basic definition because they are a form of compensation or benefit from employment “deferred to a later date or the happening of a future event.” Wis. Stat. § 766.01(4).

### **b. IRAs [§ 2.194]**

The definition in section 766.01(4)(a) does not refer specifically to IRAs. However, by implication of the terminable-interest rule, IRAs are not included in the definition of deferred-employment-benefit plan. The terminable-interest rule states:

[I]f the nonemployee spouse predeceases the employee spouse, the marital property interest of the nonemployee spouse in all of the following terminates at the death of the nonemployee spouse:

- (a) A deferred employment benefit plan.
- (b) Assets in an individual retirement account that are traceable to the rollover of a deferred employment benefit plan.

Wis. Stat. § 766.62(5); *see also* Wis. Stat. §§ 766.31(3), .58(7)(a), .588(1)(b)1. Subsection (b) was added to section 766.62(5) by 1993 Wisconsin Act 160, effective April 1, 1994. The passage of the amendment suggests that an IRA was not within the definition of a deferred-employment-benefit plan in the first place. The terminable-interest rule does not apply to benefits that are not within that definition. The implication is that the amendment was needed to extend the terminable-interest rule to IRAs in the case of certain rollovers because IRAs are not within the definition.

➤ **Note.** It may be assumed that the words *nonemployee spouse* mean the spouse who does not create the IRA even though, in fact, a spouse who is not employed may create an IRA.

For a discussion of the application of the terminable-interest rule to IRAs, including IRAs in existence on the effective date of 1993 Wisconsin Act 160, see section 2.202, *infra*.

### c. Stock Options [§ 2.195]

It is unclear whether employee stock options are included within the statutory definition of deferred-employment-benefit plans. As noted in section 2.187, *supra*, the definition in section 766.01(4)(a) includes “a plan, fund, program or other arrangement under which compensation or benefits from employment are expressly, or as a result of surrounding circumstances, deferred to a later date or the happening of a future event.” Section 766.01(4)(a) lists examples, including pension and profit-sharing arrangements and stock-bonus plans, but does not mention stock options.

The two main elements of the statutory definition are:

1. Compensation (or benefits); and

2. The deferral of the compensation or benefits to a later date or event.

Employee stock options are almost always compensatory in nature, but whether they provide benefits deferred to a later date is not clear. Some options are immediately exercisable at a discount, thus offering immediate benefits. Others may be exercisable at a later date; however, their value depends on the value of the stock subject to the option. Thus, whether an option holder will ever receive a benefit is uncertain.

Wisconsin courts have not considered the issue of whether stock options are deferred-employment-benefit plans under the Act. However, two cases in dissolution proceedings in Wisconsin and California may be relevant. Both *Chen v. Chen*, 142 Wis. 2d 7, 12, 416 N.W.2d 661 (Ct. App. 1987), and *Hug v. Hug*, 201 Cal. Rptr. 676 (Ct. App. 1984), note that stock options are a form of compensation, the benefits of which are postponed to a future date, and then compare them to pensions. Pensions clearly are deferred-employment-benefit plans; thus, the reasoning in *Chen* and *Hug* suggests that a court will find stock options to be a deferred-employment-benefit plan under the Act.

Stock options and the stock acquired through their exercise raise certain classification issues. Specifically, whether a stock option is within the definition of a deferred-employment-benefit plan will determine whether the formulas in section 766.62 applicable to plans that straddle the determination date (straddle plans) apply. *See infra* § 2.198.

## **C. Classification Rules [§ 2.196]**

### **1. In General [§ 2.197]**

Deferred employment benefits are subject to the classification rules of section 766.62. Section 766.62(1), based on section 13(a) of UMPA, states that a deferred employment benefit attributable to the employment of a spouse occurring after the determination date is marital property.

A deferred employment benefit attributable to employment of a spouse occurring partly before and partly after the determination date is mixed property. Wis. Stat. § 766.62(2). The benefit is apportioned between the nonmarital and marital property components according to a formula. The marital property component is determined by multiplying the entire benefit by a fraction, the numerator of which is the period of

employment giving rise to the benefit that occurred after the determination date and during marriage, and the denominator of which is the total period of employment giving rise to the benefit. *Id.*; see UMPA § 13(b); see also *supra* § 2.8 (statutory definition of during marriage). Some examples are helpful.

➤ **Example 1.** Assume that a deferred employment benefit is \$300,000, the spouse was employed while married 5 years before the determination date and 10 years after it, and the entire time of employment gave rise to the benefit. In this relatively simple case, the marital property component of the benefit is \$200,000 (\$300,000 multiplied by the fraction 10 years divided by 15 years). The balance is nonmarital property. The formula under section 766.62(2) is only used to determine the marital property component. The Act's general principles are used to determine the nonmarital property component. In this example, if a third party is named as beneficiary without the surviving spouse's consent, the nonmarital property component is deferred marital property potentially includible in the augmented deferred marital property estate subject to the election provided a surviving spouse by section 861.02. This is because the nonmarital property component would have been marital property if acquired while chapter 766 applied. See *infra* § 2.243.

➤ **Example 2.** Assume the same facts as in Example 1 above except that the spouse's employment began, while the spouses were married, 10 years before the determination date and 5 years before the plan was established. Thus, in this example, the entire period of employment is 20 years, but the first 5 years of employment did not give rise to a benefit. The marital property component of the \$300,000 benefit is \$200,000 (\$300,000 multiplied by the fraction 10 years divided by 15 years). If a third party is named as beneficiary without the surviving spouse's consent, \$100,000 (the balance of the benefit) is deferred marital property potentially includible in the augmented deferred marital property estate subject to the election provided a surviving spouse under section 861.02. See *infra* § 2.243.

➤ **Example 3.** Assume that, while married, a spouse begins employment 10 years before the determination date and that a deferred-employment-benefit plan is established on the determination date. Assume that employment giving rise to a benefit continues for 10 more years during marriage and after the determination date.

Assume that the benefit is \$300,000. The marital property component of the benefit is \$300,000 (benefit of \$300,000 multiplied by the fraction 10 years divided by 10 years).

Section 766.62(1)(b) provides a formula for calculating the marital property component in a deferred employment benefit when the employed spouse, the other spouse, or both spouses are at any time not domiciled in Wisconsin. In such a case, the benefit is mixed property. Under section 766.62(1)(b), the marital property component is the amount that results from multiplying the entire benefit by a fraction, the numerator of which is the period of employment giving rise to the benefit that occurred after the determination date and during marriage, and the denominator of which is the total period of the employment. It must be remembered that section 766.01(8) defines the term during marriage to mean a period during which both spouses are domiciled in Wisconsin, beginning at the determination date and ending at dissolution or the death of a spouse. Thus, a marital property component in a deferred employment benefit ceases to grow when one or both of the spouses are not domiciled in Wisconsin.

Consider again Example 1 above. In that example, the spouses were married for the entire time that the employment gave rise to the benefit. Five of those years occurred before the determination date and 10 years after it. If the example is altered so that 5 years after the determination date one of the spouses changes domicile from Wisconsin to another state and remains there, the marital property component of the benefit is \$100,000 (\$300,000 multiplied by the fraction 5 years divided by 15 years). The balance is nonmarital property.

➤ **Note.** Section 766.62(1)(b) was created by the 1988 Trailer Bill and does not affect rights that accrued before its May 3, 1988, effective date. Wis. Stat. § 766.03(5). Before May 3, 1988, the concept of marital domicile was a part of the Act. For a discussion of that concept, see section 13.46, *infra*.

➤ **Comment.** A time-apportionment formula is particularly useful for defined-benefit plans because those plans do not provide separate accounts detailing contributions and earnings history for each participant. A time-apportionment formula may, however, be somewhat arbitrary for defined-contribution plans that do provide account histories and that receive contributions varying in amount

over time (usually corresponding to the size of earnings). In addition, if there is inflation, dollars contributed early are worth more than dollars contributed late.

A plan's ownership or disposition provisions that conflict with section 766.62(1) or (2) are ineffective between spouses or former spouses or between a surviving spouse and a person claiming under a deceased spouse's disposition at death. Wis. Stat. § 766.62(3). Rules of federal preemption may also be relevant. *See infra* §§ 2.214–217. In some cases, state law may preclude application of the Act. *See infra* § 2.218.

## 2. Stock Options [§ 2.198]

Whether a stock option is within the definition of a deferred-employment-benefit plan, *see supra* § 2.195, will determine whether the formulas applicable to straddle plans in section 766.62 apply. Wisconsin courts have not considered these questions within the context of the Act. However, *Chen*, 142 Wis.2d 7, and *Hug*, 201 Cal. Rptr. 676—two dissolution cases discussed in section 2.195, *supra*—may be relevant.

In both *Chen* and *Hug*, the courts rejected arguments that an option granted during marriage must be entirely the holder's separate property because it could not be exercised until after dissolution. In *Hug*, the court emphasized that each case is fact-intensive, each option must be examined to determine its purpose, and a divorce court has great latitude in dividing the asset and determining a proper formula for doing so. 201 Cal. Rptr. at 679, 685–86.

In determining the amount subject to division in the dissolution, the court in *Hug* used a formula similar to that in section 766.62. *Hug* held that options that have exercise dates after dissolution should be divided in accordance with a formula, the numerator of which is the length of service from the date of commencement of service until the date of separation, and the denominator of which is the length of service from the date of commencement of service to the date when the option may first be exercised. *Id.* at 679.

In *Chen*, the appellate court said a formula need not be used to determine equitable results, but the court indicated that a formula like that used in *Hug* could be appropriate. *Chen*, 142 Wis. 2d at 14.

The Act, on the other hand, requires that the time-apportionment formulas of section 766.62 must be used if a deferred-employment-benefit plan is involved and it straddles the determination date. But a number of issues arise in applying those formulas if stock options are within the definition of deferred-employment-benefit plans.

The first issue that arises is what date should be used for the beginning of the time period in the numerator and denominator of the time-apportionment formulas. Is it the commencement of employment or the date the option is granted? When deferred-employment-benefit plans straddle the determination date, section 766.62 states that the numerator is the time of employment during marriage and after the determination date giving rise to the benefit. The denominator is the total period of employment giving rise to the benefit.

Assume a case in which employment begins before marriage and options are issued during marriage. *Hug* said the numerator should begin at the commencement of service. *Hug*, 201 Cal. Rptr. at 678. For all practical purposes under the Act, the numerator must begin on the determination date when straddle plans are involved. But assume the options were not contemplated by management or employees until shortly before their creation. *Nelson v. Nelson*, 222 Cal. Rptr. 790, 793 & n.4 (Ct. App. 1986), held that the numerator should begin with the *granting* of the option, saying that the options in *Hug* were designed to attract new employees and more generously reward past services, while the options in *Nelson* were designed so that only future increases in the value of the underlying stock could benefit the holders. Like *Hug*, *Nelson* emphasizes the need for a case-by-case analysis.

A second issue that arises in applying the time-apportionment formulas of section 766.62 to stock options is what date should be used for the end of the time period in the denominator. In *Hug*, the court said the denominator should begin on commencement of service and end on the date the option could first be exercised. *Hug*, 201 Cal. Rptr. at 678. *Harrison v. Harrison*, 225 Cal. Rptr. 234 (Ct. App. 1986), involved a plan in which options were vested upon being granted but permitted divestiture of stock received by virtue of exercise if an employee left employment for certain reasons and within a certain time of exercise. The court held that the denominator, like that in *Nelson*, should begin upon grant and end, not on exercise, but on the date the stock was no longer subject to divestment. *Id.* at 237–40.

When does the time period used in the denominator end if the holder of the option dies before the date the option may be exercised? If the terms of the option permit acceleration of exercise at the death of the holder, the denominator ends on the date of death. If acceleration is not permitted, presumably death would still be the ending point; otherwise, a nonmarital component would suddenly be created even in cases in which employment began after the determination date.

A third issue that arises is how stock acquired upon exercise of an employee stock option should be classified. If nonmarital property funds are used to pay the option price, then the stock will have both marital and nonmarital property components. The stock will also have marital and nonmarital components if an option straddles the determination date.

➤ **Example.** Assume that an employee began employment five years before marriage. Assume that three years into the marriage, options were issued and that four years later, the employee exercised the options and used inherited cash of \$1,000 to pay the option price when the stock had a fair market value of \$1,800. The gain on the transaction is \$800. Five-ninths of the stock is individual property representing the payment of the option price with individual property. If the option is within the definition of a deferred-employment-benefit plan, *see supra* § 2.195, the numerator of the formula used to apportion the gain of \$800 is the time of employment during marriage after the determination date giving rise to the benefit. In this case, that is seven years if the time of employment giving rise to the benefit is deemed to begin on the determination date. The denominator is the total time of employment giving rise to the benefit (in this case, 12 years). Thus, 7/12 of the gain of \$800 is marital property. The other 5/12 of the gain is individual property. If an analysis like that in *Nelson* is appropriate, so that the time of employment giving rise to the benefit is deemed to begin upon grant of the option, the ratios in connection with the gain change to 4/12 and 8/12, respectively.

Assume, in the above example, that the stock acquired by virtue of the option doubles in value by the date of the employee's death. If the payment of the option price with individual property funds creates an ownership interest in the stock (which should be the case), then the marital and nonmarital components will share in the appreciation on a pro rata basis. This is the rule in California. *See Walker v. Walker*, 265 Cal. Rptr. 32 (Ct. App. 1989).



As to options that may be exercised after dissolution or the death of the holder and that are assigned in whole or in part to the nonholder spouse, the nonholder spouse must pay his or her share of the option price upon exercise. *See id.* at 34.

A fourth issue that arises is whether the taxability of stock options must be considered. If options are actually assigned between the spouses, each spouse must bear his or her own tax consequences upon exercise. However, if the options are not assignable and tax consequences fall wholly on the holder, even though benefits are received indirectly by the nonholder spouse, reimbursement to the holder or holder's estate of a portion of the income-tax liability may be appropriate. *See Harrison*, 225 Cal. Rptr. at 237 n.1, 240–41.

For a discussion of the issues considered above, see *Employee Stock Option B*, *Equitable Distribution J.*, Oct. 1996, at 109.

### **3. Life Insurance Held by Plan [§ 2.199]**

Some deferred-employment-benefit plans may hold life insurance policies insuring participants. The classification of the ownership interest and proceeds of a life insurance policy insuring a spouse and held by a deferred-employment-benefit plan is determined under section 766.62, which sets forth the classification rules of deferred-employment-benefit plans, rather than section 766.61, which deals with the classification of life insurance policies. Wis. Stat. § 766.61(8).

## **D. Terminable-interest Rule [§ 2.200]**

### **1. In General [§ 2.201]**

Section 766.62(5) and section 766.31(3) provide that the marital property interest of a nonemployee spouse in a deferred-employment-benefit plan, or in assets in an IRA that are traceable to the rollover of a deferred-employment-benefit plan, terminates at that spouse's death if he or she predeceases the employee spouse. This terminable-interest rule, which has no counterpart in UMPA, represents a policy decision by the Wisconsin Legislature to preserve such benefits for the employee spouse; consequently, the nonemployee spouse has no testamentary power of disposition over any part of a deferred-employment-benefit plan

attributable to the employment of an employee spouse or over assets in an IRA traceable to the rollover of such a plan. The legislature's goal was to ensure an employee spouse full access to benefits in a deferred-employment-benefit plan or assets in an IRA traceable to the rollover of such a plan during that spouse's retirement years if he or she is predeceased by the nonemployee spouse.

The terminable interest rule does not apply in a situation in which the employee spouse murders the nonemployee spouse; in that circumstance the estate of the nonemployee spouse may claim a marital property interest in the benefits. *Hackl v. Hackl (In re Estate of Hackl)*, 231 Wis. 2d 43, 604 N.W.2d 579 (Ct. App. 1999). The amendment of section 766.62(5) is discussed below.

Does the terminable-interest rule apply to deferred employment benefits after they have been paid to the employee? By their terms, at least, sections 766.62(5) and 766.31(3) are limited to deferred-employment-benefit plans and assets in IRAs traceable to the rollover of such plans; the sections make no reference to benefits paid from the plans and not rolled over into an IRA. It appears, therefore, that once paid out, such benefits are no longer subject to the terminable-interest rule.

➤ **Example.** Assume that a spouse's deferred employment benefit has a value of \$200,000 and is entirely marital property. Assume that the employee retires, takes a lump-sum payment, and one day later the employee's spouse dies, survived by the retired employee. Assuming that the amounts received have not been reclassified by some means provided by the Act (such as a marital property agreement), the predeceasing spouse may will \$100,000 to whomever he or she desires (the \$100,000 being one half of the marital property component of \$200,000). Amounts received by the retired spouse on the day he or she retired retain the classification they had on the day they were paid out, but because these assets were not part of a deferred-employment-benefit plan on the date the nonemployee spouse died, the terminable-interest rule does not apply.

For further discussion of the application of the terminable-interest rule to IRAs, see section 2.202, *infra*.

2005 Wisconsin Act 216, section 41, added a reference in section 766.31(3)(a) to section 766.62(5) to make clear that the two sections

mean the same thing. For application of the terminable-interest rule in connection with deferred-employment-benefit plans holding deferred marital property, see section 2.243, *infra*.

Consistent with *Hackl v. Hackl*, 231 Wis. 2d 43, 604 N.W.2d 579 (Ct. App. 1999), 2005 Wisconsin Act 216, section 58, by reference to section 854.14(3m)(c), amended section 766.62(5) to provide an exception to its application if the surviving spouse is the employee spouse and that spouse murdered the nonemployee spouse. In such a case, the terminable-interest rule does not apply, and the ownership interest at the death of the decedent (murdered) spouse in any deferred employment benefit, or in assets in an IRA that are traceable to the rollover of a deferred-employment-benefit plan that has a marital property component, is equal to one-half the portion of the benefit or assets that was marital property immediately before the death of the decedent spouse. Committee Note to section 140.

## 2. IRAs [§ 2.202]

As noted in section 2.201, *supra*, sections 766.62(5)(b) and 766.31(3) provide that the marital property interest of a nonemployee spouse in assets in an IRA traceable to the rollover of a deferred-employment-benefit plan terminates at the death of the nonemployee spouse if he or she predeceases the employee spouse. *See also* Wis. Stat. §§ 766.58(7)(a), .588(1)(b)1. (statutory marital property agreements).

The terminable-interest rule was extended to IRAs by 1993 Wisconsin Act 160, effective April 1, 1994. Although there is no grandfather clause, the rule probably does not apply to an IRA if the nonemployee spouse died before April 1, 1994. If it did, constitutional problems might arise in connection with a retroactive taking of vested interests.

Is there a retroactive taking of vested interests in connection with IRAs in existence on April 1, 1994, when the nonemployee spouse predeceases the employee spouse after that date? That taking does not injure the nonemployee spouse during his or her lifetime and in all probability may be justified under the state's power to regulate marriages and dispositions at death. See the analysis in section 1.17, *supra*, in connection with deferred marital property.

Moreover, application of the rule to IRAs simply extends the policy embodied in section 766.62(5)(a), which provides a terminable interest in connection with deferred-employment-benefit plans so that those benefits are preserved in their entirety for a surviving employee spouse.

➤ **Note.** Tracing may be important in certain cases. Sections 766.62(5)(b) and 766.31(3) apply only to assets traceable to the rollover of a deferred-employment-benefit plan and then only to the nonemployee spouse's marital property interest in those assets. What if such tracing cannot be done? Does this mean the terminable-interest rule does not apply? It would appear from the language of these sections that it does not.

In addition, an entire rollover may not be subject to the terminable-interest rule. Only the portion of a rollover that is marital property is subject to the rule. A rollover from a deferred-employment-benefit plan is nonmarital property to the extent determined under the time-apportionment formulas of section 766.62 in connection with plans that straddle the determination date. *See supra* § 2.197.

➤ **Practice Tip.** Spouses who do not want the terminable-interest rule to apply to IRAs may execute marital property agreements so stating.

### 3. Stock Options [§ 2.203]

As noted in section 2.195, *supra*, although it is likely that employee stock options are included within the definition of deferred-employment-benefit plan for purposes of the Act, it is not entirely clear. Whether a stock option is within this definition will determine whether the terminable-interest rule applies if the spouse not holding the option predeceases the holding spouse.

If the employee stock option is within the definition of a deferred-employment-benefit plan, the terminable-interest rule applies if the nonholding spouse dies first. If the stock option is not within the definition, formulas like those described in the previously discussed California dissolution cases may be appropriate. *See Harrison v. Harrison*, 225 Cal. Rptr. 234 (Ct. App. 1986); *Nelson v. Nelson*, 222 Cal. Rptr. 790 (Ct. App. 1986); *Hug*, 201 Cal. Rptr. 676.

## E. Property and Valuation Questions [§ 2.204]

### 1. In General [§ 2.205]

Property and valuation questions in connection with the division of deferred employment benefits are many and complex. Section 766.62(2m) states in part: “Unless provided otherwise in a decree or marital property agreement, a mixed property deferred employment benefit shall be valued as of a dissolution or an employee spouse’s death.” This language is derived from section 13(b) of UMPA, but unlike the last sentence of section 13(b) of UMPA, section 766.62(2m) does not allow valuation questions to be settled by written consent. Spouses who wish to settle issues of that importance must do so by a marital property agreement. *See* Wis. Stat. Ann. § 766.62(2) Legis. Council Notes—1985 Act 37, § 128 (West 2009); *see also* Wis. Stat. Ann. § 766.31(7)(d), (3) Legis. Council Notes—1985 Act 37, §§ 76 to 83 (West 2009).

The quoted language of section 766.62(2m) applies only to a “mixed property” deferred employment benefit. That there is no reference to a benefit that is not mixed property is of little practical consequence, however. Under section 766.62, valuation and other questions pertaining to deferred employment benefits are left to state law. The comment to UMPA section 13 states:

There are many significant and important problems regarding employee benefits which [UMPA] does not address specifically. As a property statute, the thrust of [UMPA] is to treat an appropriate quantum of an employee benefit as marital property. From that point on, a court dealing with the matter will have before it the many other problems in the field. These include valuation problems, questions regarding the time at which an interest is to be quantified and delivered, questions relating to whether the plan is or is not in pay status, problems with respect to events affecting the plan which can occur with the passage of time, federal preemption problems, problems with respect to the claims of prior spouses, and many other problems that are now being heard on a daily basis in courts throughout the nation.... There is no consensus in the existing state of the law that justifies the formulation of more than the general policy in the section. Adopting states will already have dealt with many of these problems and [UMPA] does not alter that case law, but simply operates to establish an appropriate marital property interest. The existing body of state case law may be applied to that property interest.

Most of the difficult questions referred to in the comment to UMPA section 13 will be resolved in dissolution cases. At the employee spouse's death, the benefit amount is immediately determinable and valued. At the death of the nonemployee spouse, if the nonemployee spouse dies first, that spouse's interest in the plan terminates. With respect to dissolution, see section 11.18, *infra*.

## 2. The Property Right [§ 2.206]

The definition of property under the Act is broad and includes any interest that is present or future, legal or equitable, vested or contingent. Wis. Stat. § 766.01(15). With respect to deferred-employment-benefit plans, the Act's definition of property extends to nonvested as well as vested interests. This is consistent with equitable division principles at dissolution, *Bloomer v. Bloomer*, 84 Wis. 2d 124, 129 n.3, 267 N.W.2d 235 (1978); *Leighton v. Leighton*, 81 Wis. 2d 620, 261 N.W.2d 457 (1978), and with the treatment of deferred-employment-benefit plans in other community property states, Reppy & Samuel, *supra* § 2.19, at 73.

Deferred-employment-plan benefits are sometimes subject to conditions that, if not observed, could lead to forfeiture of benefits. For example, a participant may have to live to a certain date (even after vesting) or agree not to establish a competing business. The existence of such conditions does not mean that there is no property right until maturation; rather, the conditions simply create a valuation problem. See *Bloomer v. Bloomer*, 84 Wis. 2d 124, 267 N.W.2d 235 (1978); Reppy & Samuel, *supra* § 2.19, at 72.

## 3. Valuation [§ 2.207]

Since section 766.62 does not alter existing case law, see *supra* § 2.205, the significant case of *Bloomer v. Bloomer*, 84 Wis. 2d 124, 267 N.W.2d 235 (1978), and its progeny continue to have vitality. *Bloomer* refers to many community property principles in its discussion of three different techniques for valuing pension benefits at divorce.

➤ **Comment.** Numerous authorities discuss the valuation of deferred employment benefits. Many are cited in the comment to section 13 of UMPA and in *Bloomer*. Nathaniel Sterling, *Division of Pensions: Reserved Jurisdiction Approach Preferred*, 11 Comm.

Prop. J. 17 (1984), presents a useful discussion of the law in California and the advantages and disadvantages of using a present-valuation technique rather than a “reservation-of-jurisdiction” approach when the parties wait until the participant’s retirement and then the parties or a court determines how the retirement benefits are to be divided.

The court in *Bloomer* also observed that contributions to a retirement fund by an employer or employee after the employee’s divorce are not assets of the marital estate subject to division, and that therefore a retirement fund should be treated as if it were two funds, with only that part of the fund attributable to employment during the marriage considered in the division. *Bloomer*, 84 Wis. 2d at 127–28 n.1. Note that in a Wisconsin dissolution proceeding, the court need not divide the property between the spouses in accordance with its classification. *See infra* § 11.18.

#### **F. Written Consent [§ 2.208]**

There is no provision analogous to section 766.61(3)(e), which applies to life insurance policies, *see supra* § 2.177, that permits the nonemployee spouse to consent in writing to the designation of a third person as the beneficiary of deferred employment benefits. If a surviving nonemployee spouse fails to claim his or her former marital property interest in a deferred employment benefit paid to a third person, the nonemployee spouse may be making a gift to that person. *See infra* ch. 9 (tax consequences); *see also infra* §§ 2.211–.217 (federal preemption). A marital property agreement classifying the benefit as the participant spouse’s individual property, combined with the other spouse’s consent as required by ERISA, provides certainty for planning purposes.

#### **G. Liabilities of Plan Administrators [§ 2.209]**

Section 766.62(4) states that a deferred-employment-benefit plan administrator may make payments or take action in accordance with the plan and the administrator’s records without fear of liability. The implication is that a plan administrator may act with impunity solely in accordance with the plan and the administrator’s records (which will normally reflect the employee spouse’s instructions), even in the face of actual knowledge of an adverse claim.

## **H. Spousal Remedies [§ 2.210]**

If the employee spouse dies first after naming someone other than the surviving spouse as beneficiary of a deferred-employment-benefit plan, the surviving nonemployee spouse may have remedies under the Act, in addition to remedies that may be provided under federal legislation. *See infra* ch. 8; *see also* Wis. Stat. § 766.62(3) (rendering ineffective between spouses plan provisions that conflict with section 766.62(1) or (2)).

## **I. Federal Preemption [§ 2.211]**

### **1. In General [§ 2.212]**

Federal law may preempt state marital property laws with respect to deferred-employment-benefit plans by virtue of the federal Supremacy Clause under Article VI, Clause 2 of the U.S. Constitution, which provides that the laws of the United States are the supreme law of the land, state law notwithstanding. Preemption occurs in connection with certain federally sponsored plans that are established by Congress for federal employees and require payment of all benefits to the participants. Federal preemption also occurs in connection with certain aspects of private plans governed by ERISA.

### **2. Federal Benefits [§ 2.213]**

In two important cases, the U.S. Supreme Court applied federal preemption rules to federally sponsored retirement plans. In each case, Congress responded by amending the legislation involved to change the result. In *Hisquierdo v. Hisquierdo*, 439 U.S. 572 (1979), the Court held that the federal statute creating the Railroad Retirement Act, Pub. L. No. 93-445, 88 Stat. 1305 (1974) (codified as an amendment at 45 U.S.C. §§ 231–231v), preempted California law and that benefits under the plan had to be paid to the federal employee and could not be subjected to division under California community property laws in a divorce case. The Court also held that an offsetting award from other community property under California law could not be provided to the other spouse. At least one Wisconsin case, in a dissolution context, resulted in a similar holding. *See Pfeil v. Pfeil*, 115 Wis. 2d 502, 341 N.W.2d 699 (Ct. App.



1983). *But see Loveland v. Loveland*, 147 Wis. 2d 605, 433 N.W.2d 625 (Ct. App. 1988) (cited below). 45 U.S.C. § 231m subsequently was amended, however, to allow the treatment of railroad retirement benefits as “community property” at the dissolution of a marriage.

*McCarty v. McCarty*, 453 U.S. 210, 223 (1981), relied on *Hisquierdo* and held that a federal military-retirement statute preempted state law and prohibited the division of military-retirement pay as community property in a dissolution proceeding. Subsequently, Congress passed the Uniformed Services Former Spouses Protection Act, Pub. L. No. 97-252, 96 Stat. 718, 730–38 (1982) (codified at 10 U.S.C. § 1408), effective February 1, 1983. This act was specifically designed to overrule the result in *McCarty*. See S. Rep. No. 97-502 (1982), reprinted in 1982 U.S.C.C.A.N. 1596, 1611.

As to military-disability pay, there is a division of authority. Some cases find federal preemption. See, e.g., *Perez v. Perez*, 587 S.W.2d 671 (Tex. 1979); *Pfeil v. Pfeil*, 115 Wis. 2d 502, 341 N.W.2d 699 (Ct. App. 1983). *But see Loveland*, 147 Wis. 2d at 611 (distinguishing *Pfeil* and holding that federal preemption did not apply in dissolution proceeding involving spouse who unilaterally elected to convert military-retirement benefits into disability benefits). Others find no preemption. See, e.g., *Stroshine v. Stroshine*, 652 P.2d 1193 (N.M. 1982).

With respect to federal civil-service and foreign-service retirement statutes, there is language in *McCarty* to the effect that the federal statutes involved do not preempt state law. See *McCarty*, 453 U.S. at 230–31. A Wisconsin holding is in agreement. See *Mack v. Mack*, 108 Wis. 2d 604, 323 N.W.2d 153 (Ct. App. 1982). Similar results obtain in connection with federal-civil-service disability benefits. See, e.g., *Hughes v. Hughes*, 634 P.2d 1271 (N.M. 1981). A Wisconsin circuit court considered whether a veteran’s disability pension and civil-service pension were classified as marital property or whether federal preemption existed and precluded a division of those benefits. *Yde v. Yde*, No. 740-850 (Wis. Cir. Ct. Milwaukee County Dec. 18, 1987). In this case, the benefit recipient was receiving Medical Assistance and was required, as a condition of the Medical Assistance, to turn over his income to the veterans’ home. The court held that federal preemption precluded a division of both these benefits.

With respect to Social Security, see section 2.266, *infra*. For a useful discussion and catalog of federal plans and benefits, see Larry H.

Schwartz and David R. McClure, *Division of Federal Pension Benefits*, 11 Comm. Prop. J. 165 (1984).

### **3. Private Plans [§ 2.214]**

#### **a. In General [§ 2.215]**

Federal preemption of private plans must be considered in connection with ERISA and the Retirement Equity Act of 1984 (REA), Pub. L. No. 98-397, 98 Stat. 1426 (1984). Federal preemption is not an issue in connection with plans that are not governed by ERISA and REA. Moreover, the REA provides that ERISA cannot preempt state laws if a qualified domestic relations order (QDRO) divides a deferred employment benefit in a dissolution proceeding. *See* I.R.C. § 401(a)(13)(B).

However, in some important respects, death benefits payable under ERISA-governed plans are subject to federal preemption. *See, e.g., MacLean v. Ford Motor Co.*, 831 F.2d 723 (7th Cir. 1987). Changes made by the REA require that a defined-benefit or money-purchase pension plan provide a qualified preretirement survivor annuity for the participant's surviving spouse, I.R.C. § 401(a)(11), unless the spouse consents otherwise, I.R.C. § 417(a). In cases involving defined-benefit plans, the amount required to be paid to the nonemployee spouse exhausts all the benefits. Thus, the employee spouse has no opportunity to name a third party as beneficiary of any portion of the benefits unless his or her spouse consents pursuant to requirements set forth in the Internal Revenue Code and applicable regulations.

Defined-contribution plans, such as profit-sharing and stock-bonus plans, must also provide a preretirement-survivor-annuity benefit unless (1) the participant's death benefit is payable in full to his or her surviving spouse or (2) the surviving spouse consents otherwise and also consents to a designated beneficiary and the participant does not (or may not) elect payment of benefits in the form of a life annuity. I.R.C. § 401(a)(11)(B). Plans subject to the preretirement-survivor-annuity requirement may satisfy that requirement by providing an annuity that is the actuarial equivalent of not less than 50% of the participant's vested account balance at the time of death. I.R.C. § 417(c)(2). Consequently, in connection with defined-contribution plans, if the payments have not begun before the participant's death, the participant is free to dispose of

the remaining 50% of the account balance whether or not the spouse consents if the plan provisions permit such a disposition.

In these circumstances, federal law conflicts with Wisconsin law. Under Wisconsin law, an employee has complete power of disposition over the entire nonmarital property component (subject to the deferred marital property election) and half of the marital property component of the plan.

The REA may preempt the Wisconsin Marital Property Act completely. Even if there is not complete preemption in connection with defined-contribution plans, it seems reasonable and equitable that satisfaction of the spouse's interest under federal law simultaneously satisfies that spouse's marital property interest under the Act because the quantum of the surviving spouse's interest under the Act could never be greater than that provided under federal law, and in some cases could be less. A contrary argument is that the surviving spouse is entitled to receive 50% under federal law, that the balance may still include a marital property component, and that the spouse owns 50% of any such component. *But see* Wis. Stat. § 857.35 (requiring personal representative, other than surviving spouse, to notify surviving spouse of plan and its beneficiary only when personal representative becomes aware that more than 50% of benefits have been paid to third party).

➤ **Query.** May the nonemployee spouse consent to a third-party beneficiary by means other than a marital property agreement? Unlike section 766.61(3)(e) (dealing with life insurance policies), section 766.62 does not specifically permit spousal consents. Will federal law sanctioning consents in connection with ERISA-governed plans preempt any state law to the contrary so that a consent under the REA suffices without an accompanying marital property agreement? The answer should be yes. Clear and uniform rules in connection with naming of beneficiaries are critical to administration of plans under ERISA. *See Egelhoff v. Egelhoff*, 532 U.S. 141 (2001) (holding that ERISA preempts state law requiring automatic revocation of a beneficiary designation upon divorce).

I.R.C. § 408(g) states that in connection with IRAs, state community property laws are to be disregarded. However, rather than an example of federal preemption, I.R.C. § 408(g) appears to be a device to administer the tax laws. *See infra* § 9.12.

## **b. Nonemployee Spouse's Testamentary Power of Disposition When That Spouse Dies First**

### **[§ 2.216]**

Does a nonemployee spouse have a testamentary power of disposition over any portion of an employee spouse's deferred employment benefits when the nonemployee spouse dies first? *Boggs v. Boggs*, 520 U.S. 833 (1997), an important case that has property law and estate planning consequences and that also resolves a conflict between the Ninth and Fifth Circuits, says no.

In *Boggs*, Dorothy and Isaac Boggs had two sons. Dorothy died in 1979, leaving most of her estate to the sons. Isaac then remarried. At his retirement in 1985 (after his remarriage and six years after Dorothy's death), Isaac received three items: a lump-sum savings-plan distribution that was rolled over into an IRA, stock from an employee stock ownership plan (ESOP), and a monthly annuity. Isaac died in 1989, leaving most of his estate to his second wife, Sandra.

The sons claimed that their mother, Dorothy, had a community property interest in the undistributed benefits when Dorothy died in 1979 and that this interest passed to them under her will. Sandra resisted the sons' claims on the theory that Dorothy had no right to dispose of any interest in the retirement benefits, all of which were governed by ERISA.

The Fifth Circuit determined that ERISA's anti-alienation provision did not apply to Dorothy's community property interest in the retirement benefits, concluding that the transfer of the interest from Dorothy to her sons was not a prohibited assignment or alienation.

The Supreme Court reversed. Considering the spousal annuity first, the Court ruled that, under ERISA, the surviving spouse, unless he or she consents otherwise, is entitled to a joint and survivor annuity. A purpose of ERISA is to ensure that surviving spouses receive a stream of income. These provisions preempt state law claims to the contrary. Otherwise, a predeceasing nonparticipant spouse could divert funds designed to protect a surviving spouse.

Next, the Court turned to the other items received by Isaac at his retirement in 1985. The parties acknowledged that the sons' claims pertained to assets after distribution from the plan, which occurred six

years after Dorothy's death. The court noted, therefore, that this case did not involve the issue whether a nonparticipant spouse would have community claims to assets paid out of plans during marriage and before the nonparticipant's death.

Again the Court rejected the sons' claims. First, the Court pointed out that ERISA does not confer beneficiary status on persons because of marital or dependent status except in specifically delineated instances, such as the joint and survivor annuity and the QDRO. The Court stated that ERISA's silence with respect to a nonparticipant's right to make a testamentary transfer of plan benefits is "powerful support for the conclusion that the right does not exist." *Id.* at 847–48.

Second, the Court noted, ERISA's anti-alienation provision is designed to protect participants and their dependents during retirement years. Testamentary transfers by nonparticipants could defeat that purpose. Thus, the high court concluded that federal preemption precludes a nonparticipant spouse from making a testamentary transfer of the other spouse's retirement benefits governed by ERISA. *Id.* at 854.

The Court left unanswered whether preemption applies to assets distributed from the plan before the nonparticipant spouse's death. The probable answer is no. The ERISA provisions applied by the Court are designed to protect assets while they are in a plan, awaiting distribution at a future date. Thus, if the anti-alienation clause were treated like a spendthrift clause, it would be limited to the alienation of future payments and would not apply to distributions after they are made.

In the absence of a marital property agreement, the issue raised in *Boggs* would not arise in Wisconsin because under sections 766.31(3) and 766.62(5), the nonemployee spouse's marital property interest in a deferred-employment-benefit plan terminates at his or her death if he or she predeceases the employee spouse. In those circumstances, the nonemployee spouse has no interest in such a plan that may be subject to testamentary disposition.

However, a marital property agreement could provide that each spouse owns a "pure" marital property interest in a deferred-employment-benefit plan such that, for purposes of state law, the interest of the nonemployee spouse in the employee spouse's plan would not terminate if the nonemployee spouse predeceased the employee spouse. *See infra* § 7.149. Such a marital property agreement might be entered

into when the nonemployee spouse owns little property other than his or interest in the plan and the spouses hope that the nonemployee spouse will be able to bequeath his or her interest in the plan, thereby using his or her unified credit for federal estate tax purposes, if the nonemployee spouse predeceases the employee spouse. Yet such an agreement simply puts the spouses in the same posture as the spouses in *Boggs*. For discussion of the planning considerations involved, see sections 10.107 and 10.132–.147, *infra*.

### **c. Sufficiency of Marital Property Agreement or Divorce Settlement Agreement as Waiver of Nonemployee Spouse's Rights [§ 2.217]**

Does a marital property agreement or divorce settlement agreement suffice as a waiver of a nonemployee spouse's property rights in connection with plans governed by ERISA and the REA? As noted in section 2.215, *supra*, the REA provides that a surviving spouse must receive certain benefits under a qualified plan following the employee spouse's death unless the surviving spouse specifically waives them. A waiver of benefits acknowledging the effect of the waiver must be in writing and witnessed by a plan representative or a notary public. 29 U.S.C. § 1055(c)(2).

Assume a man names his wife as beneficiary of a deferred-employment-benefit plan and the couple subsequently divorces. The court-approved property settlement provides that each party waives any interest or claim in and to any deferred-employment-benefit plan of the other. The man dies without changing the beneficiary. His will leaves everything to his only child. Must the plan administrator pay the benefit to the named beneficiary, the ex-spouse, pursuant to the plan documents on file or should the plan administrator pay the benefit to the participant's estate because the ex-spouse waived her interest in the plan pursuant to the divorce decree and the man's estate takes because there is no alternate payee named?

Resolving a split among federal courts of appeal and state supreme courts on this issue, the U.S. Supreme Court held in *Kennedy v. Plan Administrator*, 129 S. Ct. 865 (2009) that, in these circumstances, federal preemption under ERISA requires the plan administrator to follow the plan documents and pay the ex-spouse. This is not because, as the plan

administrator argued, the divorce decree amounted to a waiver by the ex-spouse of her right to the benefits and such a waiver is not precluded under the anti-alienation provisions of ERISA. Rather (and despite the waiver), it is because requiring a plan administrator to follow plan documents allows employers to establish a uniform administrative scheme to guide processing of claims and disbursements of benefits. The participant could have named another beneficiary but did not avail himself of that opportunity.

➤ **Comment.** What are the implications of this decision for marital property purposes? In an important footnote, the Supreme Court stated that this decision “leaves open any questions about a waiver’s effect in circumstances in which it is consistent with plan documents. Nor do we express any view as to whether the Estate could have brought an action in state or federal court to obtain the benefits after they were distributed.” *Id.* at 875 n.10.

Clearly, naming a new beneficiary would cut off rights of an ex-spouse. But assume the man in the above case remarried before he died but still failed to name a new beneficiary. Assume also that the man and his new wife are at all times domiciled in Wisconsin and that a portion of the benefit accrued during the second marriage, thereby creating a marital property interest in that portion in the second spouse. Because an important purpose of ERISA is to protect surviving spouses, see discussion of *Boggs*, *supra* § 2.216, it is highly likely that the second spouse, who has not herself made a waiver, has rights that displace the rights of any other person named as a beneficiary. Those rights exceed in value any marital property rights that accrued. Note also that the Supreme Court left open questions concerning pursuit of benefits after the benefits have been paid out of the plan. Thus, even if the benefits are paid out to the ex-spouse pursuant to the plan documents, they could be pursued under ERISA and marital property theories, and once again the issue of the validity of the waiver comes into play.

As another case, assume a second marriage in which the spouses sign a marital property agreement in which each waives rights to the other’s property, and one spouse names a child of a prior marriage as beneficiary of his or her qualified plan and then dies survived by the other spouse. The following cases in connection with the validity of waivers may still be relevant.

*Pedro Enterprises, Inc. v. Perdue*, 998 F.2d 491 (7th Cir. 1993), involved an antenuptial agreement in which each of the parties waived any intestate share and any expectancy that he or she might be entitled to receive in the event of the death of the other party. The court held there was not an effective waiver because the agreement made no reference to pension benefits, and the pension plan involved was not in existence at the date of the marriage.

In *Melton v. Melton*, 324 F.3d 941 (7th Cir. 2003), the issue of waiver was raised in connection with a divorce agreement that contained a revocation of each party's interests in property of the other arising "by reason of their marital relation" and assets of the other party assigned that party by the agreement including "annuities, life insurance policies," and other financial instruments. *Id.* at 943. The waiver did not expressly refer to the husband's employee group term life insurance issued as part of a plan governed by ERISA. Finding first that ERISA preempts all state laws insofar as they may now or hereafter relate to any employee-benefit plan subject to ERISA, the court pointed out that, nevertheless, ERISA does not preempt an explicit waiver of interest by a nonparticipant beneficiary, and that one can look to the federal common law and state law to determine what constitutes a valid waiver. One formulation, said the court, mandates that a waiver be "explicit, voluntary and made in good faith." *Id.* at 945 (citation omitted). Essentially, when evaluating the effectiveness of a waiver, the court is concerned whether a reasonable person would have understood that he or she was waiving an interest in the proceeds or benefits in question. The court found no effective waiver, putting emphasis on the failure to expressly identify the husband's ERISA regulated employee group term life insurance.

*Melton* refers to *Manning v. Hayes*, 212 F.3d 866 (5th Cir. 2000), a case involving a settlement agreement in a dissolution based on the terms of the parties' prenuptial agreement. The court in *Manning* said that prenuptial agreements are often too broadly worded to be effective waivers, but the court did not rule out the possibility that an agreement containing an effective waiver could be presented in a future case.

## **J. State Law [§ 2.218]**

Provisions of state or municipal deferred-employment-benefit plans may in effect preempt state community property laws by insisting that



benefits be paid in their entirety to the participants. *See* Reppy & Samuel, *supra* § 2.19, at 74. Plans sponsored by a state or a municipality must be examined with this in mind.

The Wisconsin Marital Property Act may not affect certain benefits payable under retirement plans administered under chapter 40, which deals with certain persons employed by the state of Wisconsin. A document issued several years ago by the Department of Employee Trust Funds (ETF) in question-and-answer form and entitled “Effects of Divorce Judgments on WRS Benefits” stated on page 2:

Are the Chapter 40, Stats., programs administered by the ETF subject to the Marital Property Act, 1983 Wisconsin Act 186, effective January 1, 1986?

No. There is no mention of Chapter 40 or the ETF in the Act. A longstanding rule of statutory construction followed in Wisconsin states that statutes do not apply to the state unless the state is explicitly included therein by appropriate language.

*State ex rel. Department of Public Instruction v. ILHR*, 68 Wis. 2d 677, 681–82 (1975).

The statement quoted above does not appear in the current circular dealing with this subject issued by the ETF. *See* ETF, How Divorce Can Affect Your WRS Benefits (May 2004), available at <http://etf.wi.gov/publications/et4925.pdf>.

In *Jackson v. Employee Trust Funds Board*, 230 Wis. 2d 677, 602 N.W.2d 43 (Ct. App. 1999), a state employee named her sister as beneficiary of her state retirement benefits. That designation remained unchanged after her marriage. The surviving spouse claimed a marital property interest in the benefits but failed to assert remedies under the Act within the applicable statutes of limitation. The sister resisted. The issue was whether the ETF could honor a beneficiary designation that transferred marital property to a third party. The court held that the employee spouse had the right to manage and control the benefits, which includes the right to name a beneficiary. Whether a surviving spouse may have rights under the Act, said the court, was a question for another day and another forum.

## K. Deferred Marital Property [§ 2.219]

For application of deferred marital property rules to deferred-employment-benefit plans, see sections 2.243 and 12.69, *infra*.

## XIII. Marital Property [§ 2.220]

### A. In General [§ 2.221]

Deferred marital property is not a classification of property. It is a concept that provides the basis for an elective right granted a surviving spouse under section 861.02.

Deferred marital property exists whenever a spouse (who dies with a Wisconsin domicile) acquires property while married and while chapter 766 did not apply, if that property would have been marital property had chapter 766 then applied. Presumably, property acquired by the decedent spouse during marriage and after the determination date that is traceable to deferred marital property is also deferred marital property. *See* Wis. Stat. § 766.31(8); *see also supra* §§ 2.154 (tracing of predetermination date property), .8 (statutory definition of during marriage).

Deferred marital property is the basis for an election permitted to be made by the surviving spouse. *See* Wis. Stat. § 861.02. In certain cases, the election under section 861.02 may be waived, Wis. Stat. § 861.10, or diminished by a surviving spouse's prior consent, Wis. Stat. § 861.05(1)(c). For an explanation of the full operation of the election, see sections 12.136–.147, *infra*.

Note that under the Act, the deferred marital property concept does not apply at dissolution but only at the death of a spouse survived by the other spouse.

Sections 2.222–.246, *infra*, consider (1) the policy underlying the concept of deferred marital property and the election based on that concept, (2) the definition of deferred marital property, and (3) some examples of deferred marital property.

## B. Origin and Underlying Policy [§ 2.222]

The deferred marital property election is designed to avoid constitutional problems attending any effort to alter existing rights in property acquired before the Act first applies to a couple. UMPA §§ 17 cmt., 18 cmt. Thus, the election is postponed until death, which, according to the comments to sections 17 and 18 of UMPA, is an event in which the state's interest in succession of property justifies state intervention.

A second policy underlying the election based on deferred marital property is to protect the surviving spouse of a person who died domiciled in Wisconsin. The Act repealed the statutory one-third elective share previously provided by sections 861.01–.11 (1983–84). *See* 1983 Wis. Act 186, §§ 76–81. Elective rights based on deferred marital property are designed to compensate for this repeal.

This second policy is similarly served when both spouses change their domiciles to Wisconsin from other jurisdictions. For example, spouses who change their domiciles to Wisconsin from a common law state lose the protection furnished by dower, curtesy, or other elective right provided by the law of that common law state. To compensate for the loss of dower, curtesy, or other elective right against the deceased spouse's property resulting from such a change of domicile, the elective right based on deferred marital property is provided to the surviving spouse. The comment to section 18 of UMPA makes this clear. Note, however, that UMPA section 18 provides an *ownership right* in a surviving spouse in contrast to the *elective right* provided under section 861.02. UMPA section 18 provided the basis for the deferred marital property rule in former section 766.77 (repealed by the 1985 Trailer Bill). *See also infra* § 12.2.

California and Idaho first devised the deferred marital property concept; such property is referred to in those states as *quasi-community property*. *See* Cal. Prob. Code § 201.5 (West 1956); Idaho Code §§ 15-2-201 to 15-2-209 (1979). The quasi-community property rule is designed to protect spouses who move to California or Idaho from other jurisdictions. The California Probate Code was amended effective January 1, 1985. *See* Cal. Prob. Code §§ 66, 101, 102 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009–2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 19 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot).

California retained the quasi-community property rule, but the previous requirement for an election against the will was eliminated by repealing section 201.7 of the California Probate Code (Deering 1974). Several community property states apply quasi-community property concepts at dissolution as well. *See, e.g.*, Cal. Fam. Code §§ 125, 2581 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009–2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 19 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot); Ariz. Rev. Stat. § 25-318 (West, WESTLAW current through the Sixth Special Session, and legislation effective April 27, 2010 of the Second Regular Session of the Forty-Ninth Legislature (2010)).

California and Idaho extended the quasi-community property concept at death to nonprobate assets. This extension has the effect of preventing arrangements, deliberate or otherwise, that would defeat elective rights limited to probate assets. Thus, in Idaho, the augmented estate concept found in the Uniform Probate Code applies to quasi-community property placed in nonprobate arrangements. *See* Idaho Code §§ 15-2-201 to 15-2-209 (West, WESTLAW current through (2010) Chs. 1-359 and HJR 4, 5 and 7 that are effective on or before April 12, 2010); *see also* Cal. Prob. Code §§ 66, 101, 102 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009–2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 19 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot).

### C. Definition [§ 2.223]

The election permitted by section 861.02 applies only to property that meets the definition of deferred marital property. Section 851.055 defines *deferred marital property* as follows:

“Deferred marital property” means any property that satisfies all of the following:

- (1) Is not classified by ch. 766.
- (1m) Is not classified as individual property or marital property under a valid marital property agreement, unless the marital property agreement provides otherwise.
- (2) Was acquired while the spouses were married.
- (3) Would have been classified as marital property under ch. 766 if the property had been acquired when ch. 766 applied.

➤ **Historical Note.** Before section 851.055 was amended by the 1988 Trailer Bill and the legislation enacting the new Probate Code, 1997 Wisconsin Act 188, deferred marital property was defined as “property acquired during marriage and before the determination date which would have been marital property under ch. 766 if acquired after the determination date.” The current definition differs from the old definition in two respects. First, the words “while the spouses were married” were substituted for the words “during marriage.” Second, references to the determination date were deleted and replaced by the concept of periods when chapter 766 does or does not apply. The new definition is intended to expand the old definition to include periods after the determination date in which one or both of the spouses are not domiciled in Wisconsin. Thus, the phrase “while the spouses were married” used in section 851.055 must not be confused with the definition of during marriage in section 766.01(8). The phrase *while the spouses were married* includes periods when a spouse is not domiciled in Wisconsin. The phrase during marriage does not include such periods. *See supra* § 2.8.

Under the current definition, property must meet four requirements to qualify as deferred marital property:

1. The property is not classified by chapter 766. Thus, the property must have been acquired while chapter 766 did not apply or, presumably, be traceable to property acquired while chapter 766 did not apply. *See Wis. Stat. § 766.31(8); see also supra* § 2.154.
2. The property is not classified as individual property or marital property by a marital property agreement.
3. The property must have been acquired while the spouses were married. Property acquired before marriage is not deferred marital property, although such property could become deferred marital property through mixing or other means provided by the Act.
4. It must be the case that the property would have been marital property had chapter 766 applied to the spouses when the property was acquired.

Chapter 766 applies after the determination date and only while both spouses are domiciled in Wisconsin. Deferred marital property must be acquired while the spouses are married and before the actual

determination date. There can be more than one actual determination date. *See* § 2.8, *supra*. An asset acquired (or traceable to an asset acquired) while a couple is married and before an actual determination date is deferred marital property if the asset would have been marital property if, hypothetically, chapter 766 had then applied.

Deferred marital property is a part of the *augmented deferred marital property estate*, a term defined in section 861.02(2)(b) as follows:

(b) The augmented deferred marital property estate is the total value of the deferred marital property of the spouses, irrespective of where the property was acquired, where the property was located at the time of a relevant transfer, or where the property is currently located, including real property located in another jurisdiction. It includes all types of property that fall within any of the following categories:

1. Probate and nonprobate transfers of the decedent's deferred marital property under section 861.03(1) to (3).
2. Decedent's gifts of deferred marital property made during the 2 years before the decedent's death under section 861.03(4).
3. Deferred marital property of the surviving spouse under section 861.04.

Property in the augmented deferred marital property estate is subject to a surviving spouse's right to elect an amount equal to no more than 50% of the augmented deferred marital property estate. Wis. Stat. § 861.02(1). For details, see chapter 12, *infra*.

➤ **Example.** Assume that a couple's determination date is January 1, 1986, and that both spouses are domiciled in Wisconsin at all times. If while married one of the spouses acquired and fully paid for an asset with his or her compensation in the year 1965, that acquisition would have been marital property if chapter 766 had then applied to the spouses' property. If the acquiring spouse dies owning that predetermination date property (or property traceable to it) and is survived by the other spouse, the property is deferred marital property in the decedent's probate estate, which in turn is part of the augmented deferred marital property estate described in section 861.03, subject to the surviving spouse's elective rights under section 861.02, unless those rights were waived under section 861.10. If the decedent spouse had, without his or her spouse's consent, placed the asset acquired in 1965 in a nonprobate arrangement described in section 861.03, the asset would be deferred marital property passing by nonprobate means at the decedent's death, in the augmented

deferred marital property estate, and subject to the election provided by section 861.02.

➤ **Note.** Section 851.055(1m), which provides that deferred marital property cannot include property classified as individual property or marital property under a marital property agreement unless that agreement states otherwise, recognizes that property classified by a marital property agreement could be treated as deferred marital property if the agreement so specifies. Committee Note to section 60.

## **D. Characteristics [§ 2.224]**

### **1. In General [§ 2.225]**

Other characteristics of deferred marital property are found in the election set forth in sections 861.02–.06. Some of these characteristics are inherent in a statutory scheme providing an election.

### **2. Election Pertains Only to Surviving Spouse [§ 2.226]**

The election provided in section 861.02 is available only to the surviving spouse. Wis. Stat. § 861.02(1). Thus, a *decedent* spouse has no testamentary power of disposition over deferred marital property assets acquired (or traceable to assets acquired) by the surviving spouse.

Nor does the decedent spouse's estate have elective rights in the surviving spouse's property, although deferred marital property held by the surviving spouse is first used to satisfy the surviving spouse's election if made. Wis. Stat. § 861.06(2)(a). That only the surviving spouse (or that spouse's guardian) may elect under section 861.02 is consistent with the notion in section 18 of UMPA and its comment that the deferred marital property concept is designed to protect the survivor, not the decedent.

The election in section 861.02 is like the quasi-community property concept on which it is based. *See supra* § 2.222. If the nonowner (usually untitled) spouse dies first, the quasi-community property rules do not apply to property owned by the surviving (usually titled) spouse.

*See Paley v. Bank of Am. Nat'l Trust & Sav. Ass'n*, 324 P.2d 35 (Cal. Ct. App. 1958).

There is one exception to the above. If one spouse murders the other, the operation of the election is essentially reversed so that the deceased spouse has the election and the surviving spouse does not. Section 854.14(3m)(d) specifies that subsections 854.14(2)(c) and (3m)(d) apply to the election of deferred marital property if the deceased spouse was unlawfully killed by the surviving spouse. Section 854.14(3m)(d) provides that if the surviving spouse unlawfully kills the deceased spouse, then the deceased spouse's estate has the right to elect no more than 50% of the augmented deferred marital property estate as determined under section 861.02(2) as though the deceased spouse was the survivor and the surviving spouse was the decedent.

➤ **Note.** The section does not use the word “amount” but instead refers to 50%. This is probably unintentional and a court may well hold that the election should be in terms of an amount rather than a fractional share of the assets making up the augmented deferred marital property estate.

### **3. Interest Is Elective, Not Vested [§ 2.227]**

A surviving spouse does not automatically become vested with an interest in deferred marital property at the death of the titled spouse. Rather, the right to an interest in deferred marital property is made elective under section 861.02. This stands in contrast to the system envisioned under section 18 of UMPA and section 766.77 of the Act before the 1985 Trailer Bill.

### **4. Decedent Spouse Must Die Domiciled in Wisconsin [§ 2.228]**

The election provided by section 861.02 does not apply unless the decedent spouse dies domiciled in this state. Wis. Stat. § 861.02(7)(a). Consequently, section 861.02 does not apply to property or property arrangements of a spouse who dies domiciled in a jurisdiction other than Wisconsin.



If a spouse dies domiciled in Wisconsin, the surviving spouse, even if domiciled in another jurisdiction, may make the election under section 861.02 (unless waived under section 861.10).

## **5. Election Not Applicable If There Is Complete Divestment More Than Two Years Before Death**

### **[§ 2.229]**

The augmented deferred marital property estate subject to the election provided by section 861.02 does not include gifts of deferred marital property and transfers of certain property rights made more than two years before the decedent's death. Wis. Stat. § 861.03(4).

➤ **Example.** Suppose that, before or after chapter 766 applies to the spouses and more than two years before death, a spouse makes an outright gift to a third person of property that was acquired while the spouses were married and while chapter 766 did not apply but that would have been marital property if acquired while chapter 766 applied. Even if the gift exceeds the dollar amounts described in section 766.53, the election provided in section 861.02 is not available for such gift property because it is not property that could become part of the augmented deferred marital property estate.

A result similar to that in the example above obtains when deferred marital property is transferred to irrevocable trusts before or after chapter 766 applies and the transferor spouse does not retain an interest at death described in section 861.03(3). Premiums paid with marital property funds while chapter 766 applies in connection with irrevocable life insurance trusts can pose a problem. *See infra* ch. 10.

## **E. Examples [§ 2.230]**

### **1. In General [§ 2.231]**

The deferred marital property rules are best illustrated by applying them to different kinds of assets. Probate assets are considered first in sections 2.232–.238, *infra*, and then nonprobate asset arrangements are considered briefly in sections 2.239–.245, *infra*. How the rules apply to joint tenancy property is considered in sections 2.254–.260, *infra*. For

purposes of the following examples, the term determination date means the date when chapter 766 first applies to the spouses involved, and unless expressly stated otherwise, it is assumed that both spouses remain domiciled in Wisconsin after their determination date.

## **2. Probate Assets Generally [§ 2.232]**

### **a. Titled Assets [§ 2.233]**

➤ *Example.* Assume that a wife fully purchases real estate with her wages while married but before chapter 766 applies; that she takes title in her name; and that she dies while chapter 766 applies, still holding title to the asset and survived by her husband. The asset would have been marital property had chapter 766 applied at the date of its purchase. On the wife's death, the value of the real estate will be included in the augmented deferred marital property estate, against which the husband will have elective rights under section 861.02, unless he waived the election under section 861.10. If the husband had predeceased the wife, however, he would not own any interest in the real estate subject to administration (and would not have acquired any under predetermination date law); thus, he would not be able to dispose of any of the real estate at his death.

### **b. Accumulated Income [§ 2.234]**

Because under the Act all income from any source (with certain exceptions, *see supra* § 2.69, not applicable for purposes of this example) earned or accrued by a spouse during marriage and after the determination date is marital property, income earned or accrued by a spouse while married and while chapter 766 does not apply is potentially deferred marital property at death. A unilateral statement is not retroactive and cannot apply to predetermination date income. *See supra* § 2.75.

➤ *Example.* Suppose that before chapter 766 applies a wife inherits stock subject to a dividend reinvestment plan and that her dividends are reinvested in additional shares before chapter 766 applies but while she is married. If the wife predeceases her husband while chapter 766 applies and while domiciled in Wisconsin, the additional

shares (and assets traceable to those shares) acquired before chapter 766 applied and still owned by her at her death are deferred marital property, and their value will be included in the augmented deferred marital property estate, against which the husband will have elective rights under section 861.02, unless he waived elective rights under section 861.10.

**c. Assets Mixed Because of Money Expended  
[§ 2.235]**

**(1) When Tracing Is Possible [§ 2.236]**

➤ *Example.* Assume that while married and before chapter 766 applies a wife uses both her salary (which would have been marital property had chapter 766 then applied) and inherited cash (which would have been individual property had chapter 766 then applied) to fully purchase real estate titled in her name. Also assume that records permit tracing to the inherited cash. The component of this mixed asset attributable to the wife's salary is deferred marital property because it would have been marital property if chapter 766 had applied to the spouses' property at the date of acquisition. If the wife predeceases her husband while chapter 766 applies and while domiciled in Wisconsin, still holding title to the real estate (or assets traceable to it), the value of that component will be included in the augmented deferred marital property estate, against which the husband will have elective rights under section 861.02, unless he waived the election under section 861.10. *See infra* § 3.15 (direct tracing of commingled financial accounts).

How much of any appreciation of the real estate in the above example is also deferred marital property is a question considered in sections 3.16 and 3.31, *infra*. Note that the husband has no elective rights against the nonmarital property component that is not deferred marital property.

**(2) When Tracing Is Impossible [§ 2.237]**

➤ *Example.* Assume that while married and before chapter 766 applies, a wife fully purchases an asset, in part with money that would have been marital property if chapter 766 had then applied and in part

with inherited cash. Although she takes title in her name, she retains no evidence to document the sources of payment other than proof of the date of acquisition, and the methods of tracing described in chapter 3, *infra*, are of no assistance. Assume that the wife dies in 1990 domiciled in Wisconsin, still owning the asset, and that her husband survives her. Under section 861.02(2), if the presumption under section 766.31(2) that all property of spouses is marital property is overcome, the property is presumed to be deferred marital property. In this case, the presumption that the asset is marital property is overcome because there is proof that it was acquired before the determination date. However, no proof of the source of funds used to purchase the asset was retained. Thus, under section 861.02(2) the entire asset is presumed to be deferred marital property included in the augmented deferred marital property estate subject to the election in section 861.02 if the husband survives and has not waived the election under section 861.10.

➤ **Comment.** The above result may present difficulties to spouses who have not kept records during the full course of their marriage and who did not contemplate when assets were acquired that the existing law would be changed so dramatically.

#### **d. Appreciation [§ 2.238]**

The appreciation of predetermination date property is treated in detail in sections 2.149–.153, *supra*.

Substantial appreciation of either spouse's predetermination date property as a result of substantial undercompensated labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity (generally referred to in this chapter as *efforts*) of either spouse applied while married and while chapter 766 did not apply is deferred marital property subject to election at the owner's death if the owner at death (1) has a Wisconsin domicile, (2) still owns the asset (or assets traceable to it) or otherwise made it a part of the augmented deferred marital property estate under section 861.03, and (3) is survived by his or her spouse. See *supra* § 2.152. If the tests of section 766.63(2) are not met, appreciation of predetermination date property as a result of market conditions or effort of either spouse is deferred marital property only if the underlying predetermination date property is deferred marital property; but if the underlying predetermination date property is not

deferred marital property, such appreciation is also not deferred marital property. *See supra* § 2.153. If the appreciation accrues on mixed property, it must be apportioned. Substantial appreciation of either spouse's predetermination date property as a result of substantial undercompensated efforts of either spouse applied during marriage and after the determination date is not deferred marital property; rather, such appreciation is marital property. *See supra* § 2.151.

### **3. Nonprobate Assets Generally [§ 2.239]**

#### **a. In General [§ 2.240]**

A spouse may place deferred marital property, in all its manifestations, into many types of nonprobate arrangements involving third parties while retaining an interest. Such arrangements include life insurance policies, deferred-employment-benefit plans, joint tenancies, and various trusts. If the other spouse has not consented to the arrangement, then deferred marital property held in such a nonprobate arrangement is part of the augmented deferred marital property estate subject to the deferred marital property election under section 861.02. *See infra* §§ 12.136–.147 (detailed discussion of deferred marital property estate election, including trust arrangements).

#### **b. Predetermination Date Joint Tenancy Between Spouse and Third Party [§ 2.241]**

Whether created before or after the determination date, a joint tenancy created by a spouse or spouses with a third party retains all its traditional joint tenancy incidents to the extent that they differ or conflict with other incidents of classification in chapter 766. Wis. Stat. § 766.60(4)(a). Thus, a surviving third-party joint tenant's right of survivorship is recognized, but deferred marital property in such a joint tenancy and all its appreciation (other than that subject to the other spouse's rights of reimbursement) are potentially part of the augmented deferred marital property estate subject to election under section 861.02.

If marital property is added to a joint tenancy arrangement with a third party created before (or after) the determination date, a gift is made to the third party; the incidents of the joint tenancy prevail, including the

right of survivorship, to the extent that there is a conflict with other incidents of classification in chapter 766, but rights of reimbursement are provided a nontenant spouse who did not act together with the tenant spouse when the addition (gift) was made. *See* Wis. Stat. §§ 766.60(4)(a), .70(6)(c); *see also infra* §§ 2.255, 8.56.

### **c. Life Insurance Policies [§ 2.242]**

The deferred marital property rules apply to life insurance policies and may have retroactive effect because the deferred marital property component of a life insurance policy is potentially part of the augmented deferred marital property estate subject to election under section 861.02. *See* Wis. Stat. § 861.03(2)(c). Consequently, the formulas and rules described in section 2.169, *supra*, must be considered again.

A formula-based system of mixed property is developed in section 766.61 to determine how much of an insurance policy is marital property, depending on such factors as whether premiums are paid before the determination date or during marriage and after the determination date. *See supra* § 2.165 (statutory definition of during marriage). When applying the rules of deferred marital property to spouses who are domiciled in Wisconsin at the Act's effective date or who change domicile to Wisconsin after January 1, 1986, the rules of section 766.61 must be pushed back in time to a hypothetical determination date.

➤ **Example 1.** Under section 766.61(3)(a), a policy issued during marriage and after the determination date insuring the life of a spouse who is also the record owner of the policy is classified as marital property regardless of the source of the premiums paid. *See supra* § 2.169. Assume that a policy in the amount of \$100,000 was issued in 1975 while the spouses were married, insuring a spouse who is also the record owner and who names a third person as beneficiary. For purposes of simplicity, assume that the spouses always were domiciled in Wisconsin, that they did *not* pay premiums with marital property after December 31, 1985, and that the noninsured spouse did not consent to the designation of the third-party beneficiary. The entire policy proceeds are deferred marital property upon the insured spouse's death (if survived by his or her spouse), regardless of the source of premiums, because the proceeds would have been marital property if chapter 766 had applied to the spouses' property when the policy was issued. Wis. Stat. §§ 851.055, 766.61(3)(a). At the

insured's death (assuming no offsets against the proceeds), the proceeds are part of the augmented deferred marital property estate subject to election under section 861.02. *See* Wis. Stat. § 861.03.

The rules of section 766.61(3)(b), *see supra* § 2.170, are applied retroactively to policies insuring an owner spouse but paid for both before and after marriage occurs.

➤ **Example 2.** Suppose that an unmarried man purchased a \$100,000 life insurance policy on his life on January 1, 1971, naming a child of a prior marriage as beneficiary (and assume that the child is not named as beneficiary because of a decree, property settlement agreement, etc.). Assume that the man married again on January 1, 1978; first paid a premium from deferred marital property funds on January 1, 1981; first paid a premium from marital property funds on January 1, 1986; and died on January 1, 1991, survived by his second wife, who did not consent to the beneficiary designation. Assume that at all times the spouses were domiciled in Wisconsin. In this example, the policy was in existence for 20 years. It is useful to divide the proceeds into segments in accord with the relevant periods of time involved.

All the proceeds (assuming no offsets against the proceeds) pass pursuant to the beneficiary designation to the child of the prior marriage. Of this amount, one-half (\$50,000) represents the time the husband paid premiums from predetermination date property funds that are not deferred marital property. That time period includes 1971–77, when he was single, and 1978–80, when he was married but paid premiums from his predetermination date property funds that are not deferred marital property. The child owns this first portion (\$50,000) of the proceeds free of any claim of the surviving spouse. On January 1, 1981, the insured husband first used deferred marital property funds to pay a premium; no marital property funds were used (nor could have been used) until January 1, 1986. As a consequence, one-fourth of the proceeds (\$25,000) represents the time from the date the husband first used deferred marital property funds to pay a premium (January 1, 1981) to the date that he first used marital property funds to pay a premium (January 1, 1986). This second portion of the policy is deferred marital property included in the augmented deferred marital property estate; the child receives that portion of the proceeds subject to the surviving spouse's right of election under section 861.02. The final one-fourth of the proceeds

(\$25,000) is marital property because it represents the time from the date a premium was first paid with marital property funds to the date of the insured husband's death. As a consequence, the surviving spouse may recover \$12,500 from the child pursuant to section 766.70(6)(b)1. A failure to claim that property interest constitutes a gift from the second wife to the child. *See infra* ch. 9. The child owns the other \$12,500 free of any claim.

➤ **Practice Tip.** In circumstances such as those in Example 2 above, an appropriately drafted marital property agreement or written consent by the second wife pursuant to section 766.61(3)(e) could ensure that all the proceeds would be owned outright by the child.

The second example reveals that the formula set forth in section 766.61(3)(b) must be adapted in certain situations. Under the adapted formula, the deferred marital property component should be equal to what would have been the marital property component if chapter 766 had applied when that component was acquired, but with the important limitation that the deferred marital property fraction begins to diminish after a premium is first paid with marital property funds. Accordingly, the deferred marital property component in the policy and proceeds can be computed by multiplying the entire ownership interest and proceeds by a fraction, the numerator of which is the time from the date a premium is first paid with deferred marital property funds to the date a premium is first paid with marital property funds, and the denominator of which is the entire period the policy was in effect.

#### **d. Deferred-employment-benefit Plans [§ 2.243]**

➤ **Comment.** The following discussion does not consider rights of a surviving spouse under ERISA.

The deferred marital property rules apply to deferred-employment-benefit plans. Consequently, the deferred marital property component of a deferred-employment-benefit plan is potentially part of the augmented deferred marital property estate subject to election under section 861.02. *See* Wis. Stat. § 861.03(2)(b).

➤ **Example 1.** Assume that while married a husband commenced employment on January 1, 1976, and participated in a deferred-



employment-benefit plan from that date to January 1, 1991. The husband named a child of a prior marriage as beneficiary. Assume that no divorce decree is involved and that the spouses are at all times domiciled in Wisconsin, and ignore the federal rules under the Retirement Equity Act of 1984. With respect to federal preemption, see section 2.215, *supra*. If the second wife survives the husband and had not previously consented to the beneficiary designation, she may elect under section 861.02 to treat two-thirds of the benefit as part of the augmented deferred marital property estate and elect an amount up to one-half in value. She has a former marital property interest in the other one-third, which she can pursue under section 766.70(6)(b)1. See *infra* §§ 8.53–.55.

➤ **Example 2.** Assume the facts presented in Example 1, but further assume that the husband, while single, was also employed and participated in the deferred-employment-benefit plan for five years before his marriage, which occurred on January 1, 1976. On these facts, the one-fourth of the benefit representing the five years of employment before marriage is not subject to the wife's elective rights. One-half of the benefit representing the husband's time of employment from January 1, 1976, to January 1, 1986, is part of the augmented deferred marital property estate subject to the second wife's election under section 861.02. She could pursue her former marital property interest in the final one-fourth of the benefit, which represents her husband's time of employment from January 1, 1986, to January 1, 1991, under section 766.70(6)(b)1. The balance is owned by the husband's designated beneficiary.

To determine the deferred marital property component in a deferred-employment-benefit plan, it is necessary to adapt the formula in section 766.62(2). Under the adapted formula, the deferred marital property component should be equal to what would have been the marital property component if chapter 766 had applied to the spouses' property when that component was acquired, but with the important limitation that the deferred marital property fraction begins to diminish after a marital property component arises (at the determination date). Accordingly, the deferred marital property component can be computed by multiplying the entire benefit by a fraction, the numerator of which is the period of employment giving rise to the benefit that occurred while the spouses were married and before the determination date and the denominator of which is the total period of employment.

Section 861.05(1)(e) deals with the reverse order of death, that is, with what the consequences are in connection with the election if the nonparticipant spouse dies first, given that under the augmented approach the assets of both spouses are considered when determining the amount subject to election of the surviving spouse. Under section 861.05(1)(e), the interest of a nonparticipant spouse in a deferred-employment-benefit plan that is also deferred marital property is not part of the augmented deferred marital property estate. The Committee Note explains that since deferred marital property cannot exist within a deferred-employment-benefit plan unless it would have been marital property if chapter 766 had applied at its acquisition, the accompanying terminal-interest rule should also apply as if chapter 766 had applied. Committee Note section 187.

### **e. Appreciation [§ 2.244]**

Generally, the value of property included in the augmented deferred marital property estate is determined as of the decedent's death. *See* Wis. Stat. § 861.05(2)(a); *see also* Wis. Stat. § 861.05(2)(b)–(d) (exceptions to this rule). This rule catches all appreciation, regardless of source, on deferred marital property included in the augmented marital property estate. However, not all appreciation of predetermination date property that is deferred marital property in nonprobate arrangements involving third parties is also deferred marital property. Hence, determination of a decedent's augmented deferred marital property estate may require a case-by-case analysis. For example, substantial appreciation of deferred marital property in nonprobate arrangements as a result of substantial undercompensated spousal efforts applied during marriage and *after* the determination date is not deferred marital property within the meaning of section 851.055 and hence should not be part of the augmented deferred marital property estate. Rather, such appreciation, like an addition of marital property to the arrangement, is subject to (1) the other spouse's remedies under provisions such as section 766.70(6)(b) and (c), and (2) the dollar amounts applicable to gifts under section 766.53. *See infra* § 8.45; *see also supra* § 2.8 (statutory definition of during marriage).

➤ **Query.** Assume that identifiable predetermination date property that is not deferred marital property is used to fund a nonprobate arrangement involving a third party. If there is substantial appreciation as a result of substantial undercompensated spousal

efforts applied *before* the determination date, will that appreciation be included in the augmented deferred marital property estate? The answer is yes. *See* Wis. Stat. §§ 851.055, 861.05. The appreciation is deferred marital property in which the spouse retained an interest. Because it is deferred marital property, it is subject neither to the dollar amounts with respect to gifts under section 766.53 nor to the remedy provisions of subsections 766.70(6)(b) and (c).

Whether it accrues before the determination date or during marriage and after the determination date, appreciation (other than substantial appreciation that results from substantial undercompensated spousal efforts) of identifiable predetermination date property that is not deferred marital property is also predetermination date property that is not deferred marital property. Consequently, it is not subject to a section 861.02 election.

#### **f. Accumulated Income [§ 2.245]**

A number of the arrangements described in section 861.05 might permit the accumulation of income while spouses are married and before the determination date. Generally, accumulated income is deferred marital property to the extent that it would have been marital property if acquired during marriage and after the determination date. *See supra* § 2.8 (statutory definition of during marriage). With certain exceptions, section 861.05 states that deferred marital property is valued as of the date of, or immediately before, the decedent's death. The word *valued* presumably includes unwithdrawn (and, in most cases, reinvested) income. The unilateral statement permitted by section 766.59 is not available because such a statement is prospective only and cannot be made effective before the determination date.

#### **F. Move from Common Law State [§ 2.246]**

The deferred marital property concept and the election in section 861.02 are designed in part to protect surviving spouses from disinheritance after spouses change their domiciles to Wisconsin from common law jurisdictions after January 1, 1986. *See supra* § 2.222. In Wisconsin, the Act eliminates the right to elect one-third of a decedent's net probate estate. *See supra* § 2.222. In addition, if both spouses change their domiciles to this state from a common law jurisdiction, the

surviving spouse loses the protection furnished him or her by dower, curtesy, or other elective right provided by the law of that common law state. If only one spouse changes domicile to Wisconsin, see section 13.15, *infra*.

➤ **Example.** Assume that a couple changes domicile from a common law state to Wisconsin. In the absence of elective rights protecting a surviving spouse, the wife has no rights upon her husband's death to elect a share of the property accumulated in her husband's name during their marriage in the common law jurisdiction if her husband chooses to will all his property to a third party. In such a case, the wife's rights are limited to her marital property interests accumulated after the change of domicile to Wisconsin.

To make up for the loss of elective rights resulting from a change of domicile to Wisconsin and the Act's elimination of the right to elect a share of a decedent's property, the deferred marital property election under section 861.02 is provided for surviving spouses.

Thus, assets accumulated in another jurisdiction that would have been marital property under Wisconsin's approach if acquired during marriage and after the determination date are deferred marital property subject to a surviving spouse's elective rights under section 861.02. *See supra* § 2.8 (statutory definition of during marriage). These elective rights have the greatest impact when spouses change domicile from a common law state to Wisconsin. The impact is much less if the change in domicile is from a community property jurisdiction to Wisconsin. However, income accumulated by a spouse while married in an American-rule community property state, where income from separate property is separate, is apparently potentially deferred marital property subject to election after a change of domicile to Wisconsin. In Wisconsin, such income would have been marital property if acquired during marriage and after the determination date.

## **XIV. Optional Forms of Holding Property [§ 2.247]**

### **A. In General [§ 2.248]**

Section 766.60 establishes optional forms of holding property. These are not classifications under the Act.

## **B. Marital Property in “or” Form or “and” Form [§ 2.249]**

Spouses may hold marital property in a form that designates the holders by the words “(name of one spouse) or (name of other spouse) as marital property.” Wis. Stat. § 766.60(1). Spouses may also hold marital property in an “and” form. Wis. Stat. § 766.60(2). The primary difference between the two forms involves rights of management and control. *See infra* ch. 4. Use of either form does not, in itself, create a survivorship interest; if survivorship is desired, the words “survivorship marital property” should be used instead of “marital property.” *See* Wis. Stat. § 766.60(5)(a); *see also infra* § 2.250.

## **C. Survivorship Marital Property [§ 2.250]**

If the words “survivorship marital property” are used instead of “marital property” on a document of title in either of the forms described in section 766.60(1) or (2), *see supra* § 2.249, the marital property so held is survivorship marital property. Wis. Stat. § 766.60(5)(a). Whether a spouse holding marital property in his or her own name may unilaterally reclassify the property to survivorship marital property is discussed in section 4.28, *infra*.

Except as provided in a marital property agreement, if a document of title, instrument of transfer, or bill of sale expresses an intent to establish a joint tenancy exclusively between spouses after the determination date, the property is survivorship marital property. Wis. Stat. § 766.60(4)(b)1.a. It apparently makes no difference whether the assets used for this purpose were originally individual property, predetermination date property, or marital property.

A joint tenancy exclusively between spouses that is given to the spouses by a third party after the determination date is survivorship marital property unless the donor provides otherwise. Wis. Stat. § 766.60(4)(b)2. As to the characteristics of joint tenancies created between spouses, given to spouses by third parties, or created between spouses and third parties, see sections 2.253–.260, *infra*.

Homestead property acquired after the determination date will, in most cases, be survivorship marital property. *See infra* § 2.251.

The characteristics of survivorship marital property are described in section 766.60(5)(a). On the death of a spouse, that spouse's ownership rights in the property vest solely in the surviving spouse by nontestamentary disposition at death; therefore, the first spouse to die may not dispose at death of any interest in survivorship marital property.

The decedent's interest in survivorship marital property vests in the surviving spouse free of the claims of the deceased spouse's unsecured creditors. Wis. Stat. § 859.18(4)(a)1. A mortgage, security interest, or lien on the property does not defeat the right of survivorship. The surviving spouse takes the property subject to the mortgage, security interest, or lien. Wis. Stat. § 766.60(5)(b).

A judgment lien on the decedent's interest in survivorship marital property does not defeat the right of survivorship. Wis. Stat. § 766.60(5)(c). If execution of the judgment lien was issued before the spouse's death, the surviving spouse takes the decedent's interest subject to the lien. *Id.* If execution of the lien on the decedent's interest in survivorship marital property was not issued before death, the surviving spouse takes the decedent's interest free of the lien. *Id.* If the judgment lien is on both spouses' interests in the survivorship marital property and all the spouses' property was available under section 766.55 to satisfy the obligation involved, apparently the surviving spouse takes the property subject to the lien even if execution was not issued before the decedent's death. *Id.*

➤ **Query.** If property held as survivorship marital property is sold, are the proceeds also survivorship marital property? In the absence of a marital property agreement so declaring, it appears that survivorship marital property cannot exist unless there is a document of title and the document of title includes both spouses' names and the words "survivorship marital property." In the absence of those words on the check (or assets into which the proceeds are invested), the proceeds are marital property without survivorship. There are exceptions for homesteads (which are subject to special rules, *see infra* § 2.251) and expressions of intent on certain documents of title (or transfer) to create joint tenancies between spouses. *See* Wis. Stat. Ann. § 766.60(4)(b) Legis. Council Note—1985 Act 37, §§ 124 to 126 (West 2009) (ability of one spouse to unilaterally destroy right of survivorship in survivorship marital property); *see also infra* § 4.60.

## **D. Homestead Property [§ 2.251]**

Section 766.605, a provision with no counterpart in UMPA, provides that a homestead acquired after the determination date in a transaction exclusively between spouses is survivorship marital property if no intent to the contrary is expressed in the instrument of transfer or a marital property agreement. To avoid confusion, husbands and wives should refer to their homestead property as a “homestead” on the deed. If a husband and wife wish to take the property as joint tenants, they will have to do so by marital property agreement. *See* Wis. Stat. Ann. § 766.60(4)(b)1.a. Legis. Council Note—1985 Act 37, §§ 124 to 126 (West 2009).

The crucial moment is when the homestead is “titled” at the time of acquisition. Wis. Stat. Ann. § 766.605 Legis. Council Notes—1991 Act 301, § 21 (West 2009). If the title is in the names of both spouses, the homestead is survivorship marital property. If the title is in only one spouse’s name, there is no element of survivorship even if marital property assets were used to acquire the homestead. Whether a homestead titled in the name of only one spouse is classified as marital property depends on the source of the funds used to acquire the homestead.

There is some uncertainty about the status of homestead property when it is no longer used as a homestead. Presumably, it retains its attributes of the survivorship marital property form of holding because under section 766.605 those attributes are determined at the time of acquisition.

A homestead may be reclassified under section 766.31(10). Wis. Stat. § 766.605. Thus, a homestead may be reclassified by gift, conveyance signed by both spouses, or marital property agreement. In addition, a spouse can waive homestead rights under a marital property agreement. *Jones v. Estate of Jones*, 2002 WI 61, 253 Wis. 2d 158, 646 N.W.2d 280.

## **E. Concurrent Forms of Ownership [§ 2.252]**

### **1. In General [§ 2.253]**

As originally enacted, section 766.60 of the Act (optional forms of holding property; survivorship ownership) was based on UMPA section 11, which stated that spouses may hold property in any form permitted by law, including a concurrent form of holding. The comment to UMPA section 11 explained that a concurrent form was consistent with the underlying difference under UMPA between ownership and the integrated matters of holding and management and control. This comment caused confusion in Wisconsin about whether a joint tenancy, acquired with marital property funds, between a husband and wife remained marital property, possibly subject to probate when the first spouse died and to the reach of creditors under the family-purpose doctrine, or whether it was, in fact, a joint tenancy with all the characteristics set forth in section 700.17.

The 1985 Trailer Bill attempted to resolve the confusion. First, section 700.17 (classification and characteristics of certain concurrent interests) was amended by adding a reference to section 766.60(4)(b), which establishes rules for an attempt to create joint tenancies and tenancies in common exclusively between spouses after the determination date by means of a title document. Second, section 766.60(4)(a) was changed to clarify the character of joint tenancies and tenancies in common created exclusively between spouses before the determination date and between a spouse or spouses and third parties created before or after the determination date. Section 766.60(4)(a) provides:

Spouses may hold property in any other form permitted by law, including but not limited to a concurrent form or a form that provides survivorship ownership. Except as provided in [section 766.60(4)(b)] and except with respect to any remedy a spouse has under this chapter, whether a tenancy in common or joint tenancy was created before or after the determination date, to the extent the incidents of the tenancy in common or joint tenancy conflict with or differ from the incidents of property classification under this chapter, the incidents of the tenancy in common or of the joint tenancy, including the incident of survivorship, control.

Section 766.60(4)(b) deals with the attempt to create joint tenancies or tenancies in common exclusively between spouses after the



determination date by document of title, instrument of transfer, or bill of sale; consequently, those forms of ownership are not governed by section 766.60(4)(a). All other joint tenancies and tenancies in common involving a spouse are governed by section 766.60(4)(a). Except for remedies a spouse has under chapter 766, when the incidents of property classification in chapter 766 conflict with the traditional incidents of common or joint tenancies described in section 766.60(4)(a), the traditional incidents of the common and joint tenancies control. Therefore, before considering examples of the application of section 766.60(4)(a), it is useful to review some of the differences between joint-tenancy property, tenancy-in-common property, and marital property.

1. Inherent in a joint tenancy is the right of survivorship. There is no right of survivorship for tenancy-in-common property or marital property. However, when a document of title is involved, a survivorship feature may be added to marital property to create survivorship marital property. *See* Wis. Stat. § 766.60(5)(a). Also, a homestead acquired exclusively between spouses is survivorship marital property unless a contrary intent is expressed in the instrument of transfer. Wis. Stat. § 766.605; *see supra* § 2.251.
2. Either spouse may unilaterally convey a one-half interest in a joint tenancy other than a homestead to a third party. (The joint tenancy is then converted to a tenancy in common.) Similarly, either spouse may unilaterally convey his or her interest in a tenancy in common other than a homestead to a third party. A spouse may not unilaterally convey an interest in marital property. A spouse with management and control may sell a portion of a marital property asset, but the proceeds or portion remaining after the sale is still marital property. The ability to unilaterally sever the survivorship feature of survivorship marital property is discussed in section 2.257, *infra*.
3. A spouse must observe the good-faith duty when dealing with marital property. Wis. Stat. § 766.15(1). Unless there is a marital property component, there is no such good-faith duty for joint-tenancy or tenancy-in-common property.
4. During cotenants' lifetimes, an unsecured creditor of a debt-incurring tenant can reach one-half of the joint tenancy or the debtor spouse's undivided interest in tenancy-in-common property. A creditor who extended credit in the interest of the marriage or family can reach all

marital property, including all survivorship marital property, while both spouses are living. *See* Wis. Stat. § 766.55(2)(b).

5. At the death of a joint tenant, the surviving joint tenant owns the entire asset free of the claims of the deceased joint tenant's unsecured creditors. An unsecured creditor of a deceased owner of a tenancy-in-common interest can reach the deceased's undivided interest in his or her probate estate. By contrast, when an owner of marital property dies, an unsecured creditor who extended credit in the interest of the marriage or family can reach all the marital property at the death of the first owner, not just the deceased's interest. *See* Wis. Stat. §§ 859.18(2), 766.55(2)(b). As to the rights of unsecured creditors of a deceased spouse in connection with survivorship marital property, see section 2.257, *infra*.
6. The lien of a docketed judgment (based on an obligation described in section 766.55(2)) against one spouse encumbers all the marital property real estate held by the incurring spouse, and the lien continues to encumber the property on the death of either spouse. *See infra* § 4.54. (The lien of a docketed judgment based on an obligation described in section 766.55(2) incurred by one spouse does not encumber marital property real estate held by the nonincurring spouse unless the nonincurring spouse is named as a defendant in the action for which the judgment is rendered and certain tests in section 806.15(4) are met. *See* Wis. Stat. § 806.15(4).) As to judgment liens and survivorship marital property, see section 2.250, *supra*. The lien of a docketed judgment against a spouse who owns a tenancy-in-common interest in real estate encumbers the undivided interest of that tenant in common during life and at death but does not encumber the other spouse's interest. The lien of a docketed judgment against a spouse who is a joint tenant creates a lien on the debtor spouse's interest in joint-tenancy real estate; the lien does not extend to the other joint tenant's interest. If the debtor spouse dies before the judgment is executed, that spouse's interest disappears. Therefore, the lien, if not executed, also disappears; the surviving spouse, whose interest extends to the entire asset, owns all the real estate free and clear of the judgment lien. *Northern State Bank v. Toal*, 69 Wis. 2d 50, 230 N.W.2d 153 (1975).
7. As to adjustment in basis at the death of the first spouse to die, see section 9.29, *infra*.

➤ **Note.** The discussion in sections 2.254–.260, *infra*, does not deal with accounts at financial institutions governed by chapter 705. For a discussion of such accounts, see sections 2.262–.264, *infra*.

## **2. Joint Tenancies and Tenancies in Common Created Before Determination Date [§ 2.254]**

Two types of joint tenancies and tenancies in common involving a spouse may be created before the determination date: (1) joint tenancies and tenancies in common exclusively between spouses and (2) joint tenancies and tenancies in common created between a spouse or spouses and a third party. With both types, the incidents of the joint tenancy or tenancy in common control if they conflict with or differ from the incidents of property classification under chapter 766 (apart from a nontenant spouse's remedies that may exist in the second type). Wis. Stat. § 766.60(4)(a). In short, the statutory incidents of such preexisting joint tenancies and tenancies in common set forth in section 700.17 are preserved, including the right of survivorship, regardless of the classification of property held in the tenancy. See Wis. Stat. Ann. § 766.60(4)(a) Legis. Council Note—1985 Act 37, §§ 124 to 126 (West 2009). Such tenancies could presumably be reclassified by marital property agreement. Assuming no such reclassification, the question of mixing must be considered. See *infra* § 3.26.

➤ **Example 1.** Assume that a husband and wife domiciled in Wisconsin purchase property as joint tenants in 1976 subject to a mortgage. Assume that the husband uses his wages (marital property) after January 1, 1986, to pay the mortgage. Also assume that the enhancement of equity creates an ownership interest as opposed to a right of reimbursement. See *infra* § 3.41. Is the enhancement of the equity classified as marital property, survivorship marital property, or joint-tenancy property? It is marital property (thereby creating a mixed asset), but to the extent the incidents of ownership of marital property conflict with or differ from the traditional incidents of ownership of joint tenancy, the incidents of joint tenancy control, regardless of the classification of the property held in the tenancy. See Wis. Stat. Ann. § 766.60(4)(a) Legis. Council Note—1985 Act 37, §§ 124 to 126 (West 2009). Because traditional incidents of joint tenancy control, the right of survivorship is recognized, and the surviving joint tenant owns the entire asset free and clear of claims of

the deceased spouse's unsecured creditors, even credit extended in the interests of the marriage or family. Wis. Stat. § 859.18(4)(a)2. Unlike marital property, no portion of the asset is subject to probate administration in the estate of the first tenant to die.

If the incidents of marital property classification under chapter 766 do not conflict with or differ from the incidents of joint tenancy or tenancy in common, the incidents of marital property control, as illustrated in the following example:

➤ **Example 2.** Assume that an asset with a marital property component (added during marriage and after the determination date) held in a joint tenancy created exclusively between the spouses before the determination date is sold during marriage after the determination date, and the sale proceeds are deposited in an account in one spouse's name. *See supra* § 2.8 (statutory definition of during marriage). In the absence of a gift, the proceeds are apparently marital property to the extent of the marital property component that existed immediately before the sale.

➤ **Query.** When a joint tenancy involves a mixture of marital and nonmarital property, will there be an adjustment in basis of the entire marital property component for income tax purposes on the death of the first tenant spouse to die? For discussion of federal and Wisconsin basis issues when community property is held in joint tenancy, see section 9.28, *infra*.

➤ **Example 3.** Assume that a joint tenancy is created between a husband and a third party while he is married but before the determination date. Assume that the husband uses his wages during marriage, both before and after the determination date, without his wife's consent, to retire a mortgage on the property. If the husband dies first, the third party owns the entire asset. To the extent that the equity was enhanced by use of the husband's wages before the determination date, deferred marital property is created and is part of the augmented deferred marital property estate subject to election by the surviving spouse under section 861.02. The payment of the mortgage with the husband's wages after January 1, 1986, also enhanced the equity in the property. That enhancement is marital property but it passes to the third party pursuant to the rules applicable to joint tenancies. Section 766.60(4)(a) refers to remedies

provided to the other spouse. Thus, the enhancement of the equity is treated as a gift by the husband to the third party, subject to the wife's rights of reimbursement under section 766.70(6)(c). *See infra* ch. 8.

➤ **Example 4.** Assume the same facts as in Example 3, except that no gift is made; the husband (using marital property) and the third party contribute equally to the joint tenancy; the property is sold; and the husband and the third party split the proceeds. The husband's share of the proceeds is presumably marital property because no gift was made. If the husband dies before the property is sold so that the third party becomes the owner of the entire interest, the wife has a remedy under section 766.70(6)(c). If the third party dies first, the husband obtains title to the entire interest; presumably, one-half is marital property, and the other half received as a gift from the third party is the husband's individual property.

### **3. Joint Tenancies and Tenancies in Common Created After Determination Date Between Spouse or Spouses and Third Party [§ 2.255]**

➤ **Example.** Assume a joint tenancy or a tenancy in common is created between a spouse or spouses and a third party after the determination date. It is not likely that such a tenancy would include deferred marital property at the death of a spouse, but it is a possibility. The nontenant spouse has remedies of reimbursement under section 766.70(6)(c) if marital property is placed in such an arrangement and the spouses did not act together in the creation of the tenancy.

### **4. Attempt to Create Joint Tenancies and Tenancies in Common Exclusively Between Spouses After Determination Date [§ 2.256]**

#### **a. Joint Tenancies [§ 2.257]**

If a document of title, instrument of transfer, or bill of sale expresses an intent to establish a joint tenancy exclusively between spouses after the determination date, the property is survivorship marital property

under section 766.60(5). Wis. Stat. § 766.60(4)(b)1.a. In the absence of a marital property agreement requiring a different result, such an attempt to create traditional joint-tenancy property fails. It apparently makes no difference whether the property used for this purpose was originally individual, marital, or predetermination date property; the result is survivorship marital property. Because it is survivorship marital property, at the death of the first spouse to die the decedent's interest in the property vests by nontestamentary disposition in the surviving spouse. *See supra* § 2.250.

➤ **Note.** Because of the Act, section 700.19(2) (pertaining to joint tenancies between spouses) loses most of its significance. Section 700.19(2) provides that if persons named as owners in a document of title, transferees in an instrument of transfer, or buyers in a bill of sale are described as husband and wife, or are in fact husband and wife, they are joint tenants unless the intent to create a tenancy in common is expressed in the document, instrument, or bill of sale. Section 700.19(2) is generally limited to property acquired by spouses before January 1, 1986. Section 700.19(2) applies to acquisitions by spouses after January 1, 1986, only if chapter 766 does not apply when the property is acquired. For example, chapter 766 would not apply at the date of acquisition if, on that date, at least one of the spouses is domiciled outside Wisconsin.

A joint tenancy exclusively between spouses that is given to both spouses after the determination date by a third party is survivorship marital property unless the donor provides otherwise. Wis. Stat. § 766.60(4)(b)2.

➤ **Note.** Section 700.19(2) might, at first glance, appear to require a different result. Section 700.19(2) provides that if persons named as owners in a document of title, transferees in an instrument of transfer, or buyers in a bill of sale are described as husband and wife, or are in fact husband and wife, they are joint tenants unless the intent to create a tenancy in common is expressed in the document, instrument, or bill of sale. Section 700.19(2) applies, however, only to (1) property acquired by spouses before January 1, 1986, and (2) property acquired by spouses after January 1, 1986, while chapter 766 does not apply (e.g., because one or both of the spouses is domiciled outside Wisconsin).

Spouses who wish to create joint tenancies with the traditional incidents of joint tenancy after the determination date may do so by marital property agreement. Wis. Stat. Ann. § 766.60(4)(b) Legis. Council Note—1985 Act 37, §§ 124 to 126 (West 2009). It appears that a marital property agreement is the only way spouses may create traditional joint tenancies after the determination date.

A creditor is not adversely affected by the creation of a joint tenancy by marital property agreement unless the creditor has received the requisite notice under sections 766.55(4m) and 766.56(2)(c). Wis. Stat. Ann. § 766.60(4)(b)1. Legis. Council Notes—1991 Act 301, § 20 (West 2009). Consequently, in the absence of such a notice, a surviving joint tenant does not own the asset free and clear of the claims of the deceased spouse's unsecured creditors who extended credit in the interests of the marriage or family if, absent a marital property agreement, the asset would have been marital property or property of the obligated spouse.

As a matter of property law, the most significant differences between a joint tenancy as defined under section 700.17 and survivorship marital property involve rights of severance, creditors' rights during the marriage, and the basic nature of the two types of property interests.

A joint tenant (of other than a homestead) may unilaterally destroy the right of survivorship (for example, by conveying a one-half interest in the joint tenancy). In contrast, the spouse's ability to unilaterally destroy the right of survivorship in survivorship marital property other than a homestead depends first on the form in which the property is held (that is, whether in the "and" or the "or" form, *see supra* §§ 2.249, .250), and second on whether the entire item is transferred (if a spouse transfers only a portion of the survivorship marital property, the remaining portion is still survivorship marital property). *See* Wis. Stat. Ann. § 766.60(4)(b)2. Legis. Council Note—1985 Act 37, §§ 124 to 126 (West 2009); *see also infra* § 4.60.

At the death of a spouse with an interest in survivorship marital property or a joint tenancy, the survivor owns the entire asset free of the claims of the deceased spouse's unsecured creditors, even those claims incurred in the interest of the marriage or family. Wis. Stat. § 859.18(4)(a)1., 2. During marriage, however, a creditor who extended credit to one spouse in the interest of the marriage or family may reach all survivorship marital property, Wis. Stat. § 766.55(2)(b), but only half

of a joint tenancy, *Northern State Bank v. Toal*, 69 Wis. 2d 50, 230 N.W.2d 153 (1975).

As to differences in the basic nature of these two types of property interests, see section 9.30, *infra*.

For tax purposes, only one-half of a joint tenancy is subject to an adjustment in basis at the death of the first spouse to die, whereas all survivorship marital property should receive an adjustment in basis. See *infra* § 9.31.

### **b. Tenancies in Common [§ 2.258]**

If a document of title, instrument of transfer, or bill of sale expresses an intent to establish a tenancy in common exclusively between spouses after the determination date, the property is marital property. Wis. Stat. § 766.60(4)(b)1.b. In the absence of a marital property agreement requiring a different result, such an attempt to create a traditional tenancy in common fails. It apparently makes no difference whether the property used for this purpose was originally individual, marital, or predetermination date property; the result is marital property.

Under section 766.60(4)(b)2., a tenancy in common exclusively between spouses that is given to the spouses by a third party after the determination date is marital property unless the donor provides otherwise.

➤ **Note.** Section 700.18 provides that “[t]wo or more persons named as owners in a document of title, transferees in an instrument of transfer or buyers in a bill of sale are tenants in common, except as otherwise provided in s. 700.19 or ch. 766.” Chapter 766 applies otherwise through section 766.60(4)(b)2. Section 700.19(2) applies only if the title document specifies a joint tenancy or describes the tenants as husband and wife—but even then section 700.19 is of extremely limited application, because it applies to acquisitions of titled assets by spouses after January 1, 1986, and then only if chapter 766 does not apply when the property is acquired (e.g., because one or both of the spouses is domiciled outside Wisconsin).

Spouses who wish to create tenancies in common with the traditional incidents of tenancy in common may do so by marital property



agreement. Wis. Stat. Ann. § 766.60(4)(b)1. Legis. Council Note—1985 Act 37, §§ 124 to 126 (West 2009). It appears that a marital property agreement is the only way spouses may create traditional tenancies in common after the determination date.

A creditor is not adversely affected by the creation of a tenancy in common by marital property agreement unless the creditor has received the requisite notice under sections 766.55(4m) and 766.56(2)(c). Wis. Stat. Ann. § 766.60(4)(b)1. Legis. Council Notes—1991 Act 301, § 20 (West 2009). Without such notice, therefore, a creditor who extended credit in the interest of the marriage or family is not limited to the undivided interest of the debt-incurring spouse but may seek recovery from both halves of the property if, in the absence of a marital property agreement, the asset would have been either marital property or property of the obligated spouse.

Tenancy-in-common property is quite similar to marital property in many respects, including the ownership right in each half at death and the tenant's ability to dispose of 50% of the asset at death. Moreover, since 1985, the Wisconsin intestacy statutes have not distinguished between marital property and tenancy-in-common property (if there are no children from a prior marriage). The two forms of property do differ with respect to (1) creditors, *see supra* § 2.253, (2) conveyancing during the marriage, *see infra* § 2.260, and (3) the laws of intestacy if there are children from a prior marriage, *see* Wis. Stat. § 852.01(1)(a).

With respect to the last point dealing with intestacy, 2005 Wisconsin Act 216, section 65, created new section 852.01(1)(a)2.b. This new section deals with tenancy-in-common property held equally and exclusively by spouses, the interest of the deceased spouse passes by intestacy, and the deceased spouse has children by a prior marriage. The Committee Note to section 65 explains that the amendment makes treatment of such tenancies parallel to the treatment of marital property. Thus, the surviving spouse keeps his or her half, and the other half belonging to the decedent passes to his or her children. Before the amendment, says the Committee Note, there was the possibility that the surviving spouse could not only retain his or her half but also claim one half of the decedent's interest. *Id.* The amendment does not expressly deal with a decedent's interest in a tenancy in common that is in proportions other than equal or that involves ownership of a third party.

**c. Comparison [§ 2.259]**

The planner must be aware of the different consequences that flow from (1) an acquisition by a document of title, instrument of transfer, or bill of sale that expresses an intent to create a joint tenancy exclusively between spouses after the determination date and (2) an acquisition by a document of title, instrument of transfer, or bill of sale that expresses an intent to create a tenancy in common exclusively between spouses after the determination date. In the first case, without a marital property agreement, survivorship marital property results; the incident of survivorship obtains, and certain creditors of the first spouse to die may not reach the asset. In the second case, without a marital property agreement, marital property results; there is no survivorship between the spouses, one-half of the asset is subject to probate when the first spouse dies, and the creditors who have extended credit for family-purpose obligations can reach both halves of the asset upon the death of the first spouse to die.

**d. Language on Documents of Title Expressing Intent to Create Spousal Joint Tenancies or Tenancies in Common [§ 2.260]**

Section 700.19(1) provides that creation of a joint tenancy is determined by the intent expressed in the document of title. Any of the following constitutes an expression of such intent: “as joint tenants,” “as joint owners,” “jointly,” “or the survivor,” “with right of survivorship,” or any similar phrase except one similar to “survivorship marital property.” Wis. Stat. § 700.19(1).

Section 700.19(2) (which applies to joint tenancies between spouses) is generally limited to acquisitions of titled assets exclusively between spouses before January 1, 1986. Section 700.19(2) applies to acquisitions of titled assets by spouses after January 1, 1986, only if chapter 766 does not apply when the property is acquired. For example, chapter 766 would not apply at the date of acquisition if, on that date, at least one of the spouses is domiciled outside Wisconsin.

Section 766.60(4)(b)1. states that, except as provided in a marital property agreement, if an intent is expressed in a document of title, instrument of transfer, or bill of sale to create either a joint tenancy or a

tenancy in common exclusively between spouses domiciled in Wisconsin after the determination date, the property is survivorship marital property or marital property, respectively. *See supra* §§ 2.257–.258. This provision raises a question about the language needed on a document of title to express an intent to create a joint tenancy or a tenancy in common exclusively between spouses after the determination date. What if a document of title simply states “H and W as husband and wife”? If a homestead is involved, it is survivorship marital property. Wis. Stat. § 766.605. Assuming a homestead is not involved, that language on a document of title would create a joint tenancy under section 700.19(2) if the property was acquired before January 1, 1986. For property acquired after January 1, 1986, however, section 700.19(2) is inapplicable unless chapter 766 did not apply when the property was acquired. In addition, the hypothetical language described does not conform to any of the expressions catalogued in section 700.19(1) as sufficient to create a joint tenancy. However, the language described meets the definition of a tenancy in common under section 700.18. Does the hypothetical language express an intent to create a tenancy in common? If it does, that language creates marital property by virtue of section 766.60(4)(b)1.b. If not, the asset acquired may retain the classification of the property used to make the acquisition.

## **F. Accounts Between Husband and Wife [§ 2.261]**

### **1. In General [§ 2.262]**

Joint accounts are not joint tenancies. Rather they are governed by chapter 705, which deals with multiple-party and agency accounts offered by financial institutions. Chapter 705 and its relationship with the Act are discussed in sections 2.263 and 2.264, *infra*.

### **2. Joint Accounts [§ 2.263]**

A joint account is an account, other than a marital account, payable on request to one or more of two or more parties whether or not mention is made of any right of survivorship. Wis. Stat. § 705.01(4). Section 705.01(4) provides that a joint account also means any account established with the right of survivorship on or after January 1, 1986, by two parties who claim to be husband and wife, that is payable on request to either or both of the parties. *Id.*

There is a presumption that a joint account belongs, during the lifetime of all parties, to the parties without regard to the proportion of their respective contributions to the sums on deposit or to the number of signatures required for payment. Wis. Stat. § 705.03(1). The application of any sum withdrawn from a joint account by a party to the account is not subject to inquiry by any person, including any other party to the account, except that the spouse of one of the parties may recover under section 766.70 if conditions prescribed by section 766.70 are met. *Id.* At the death of a party, the account presumptively belongs to the surviving party or parties. Wis. Stat. § 705.04(1).

On the last point, *Hall v. Jung (In re Estate of Jung)*, 2000 WI App 151, 237 Wis. 2d 853, 616 N.W.2d 118, is instructive. The husband and wife executed a marital property agreement that declared, among other things, that a certain annuity was the husband's individual property. The agreement made no promises about who the beneficiary of the annuity contract had to be nor did it deal even in a general way with disposition of property at the death of a party. The husband also executed a will leaving all his individual property to his children of a prior marriage.

The annuity contract stated, however, that the wife was the co-annuitant and that upon the husband's death, the co-annuitant became the owner of the annuity. When the husband died, the wife and the children of the prior marriage all claimed the annuity. The court found that the agreement merely classified the property, and that terms of the annuity contract controlled its disposition. Thus, the annuity passed to the wife as a nonprobate transfer under section 705.20(1)(c) and, in addition, and with the same result, as a joint account under section 705.04.

Provisions protecting financial institutions are provided under section 705.06. Language sufficient to create a joint account is set forth in section 705.02.

Will nonmarital property cash be reclassified as marital property cash upon deposit into a joint account held exclusively by the spouses? Will it retain its classification after a withdrawal from the account? These questions are dealt with in several cases decided by Wisconsin Court of Appeals. As a result of these decisions, the answers are in a process of development.

In two cases, *Fowler v. Fowler*, 158 Wis. 2d 508, 518, 463 N.W.2d 370 (Ct. App. 1990), and *Lloyd v. Lloyd (In re Estate of Lloyd)*, 170

Wis. 2d 240, 269, 487 N.W.2d 644 (Ct. App. 1992), the court equated joint accounts with joint tenancies in analyzing whether assets are reclassified upon deposit into a joint account. Citing *Fowler*, 158 Wis. 2d at 518, with approval, the court in *Lloyd* stated: “Although a joint account is a statutory creation as opposed to a true common law joint tenancy, at least one Wisconsin case appears to equate the two.” 170 Wis. 2d at 256 n.4.

In *Lloyd*, for example, the court stated that a postdetermination date transfer of assets of any classification—whether individual property, predetermination date property, or marital property—into a joint account exclusively between spouses “changes the character of the ownership interest in the entire property into marital property.” *Id.* at 269 (citing *Fowler*, 158 Wis. 2d at 518). As a result, tracing is irrelevant. The court also held that marital property cash later withdrawn from the account retains its classification as marital property. *Id.* at 269–70. By the same reasoning, property placed into a joint account before the determination date while spouses are married is deferred marital property.

➤ **Comment.** The court in *Lloyd* said that when a joint account or a joint tenancy is created, each party has an equal, undifferentiated interest in the whole of the property. *Id.* at 269. This is certainly true of joint tenancies. Joint accounts, however, are governed by chapter 705. Each spouse has access to a joint account and may withdraw all the funds in that account unilaterally. *See* Wis. Stat. § 705.01(4). In connection with a joint tenancy as defined in section 700.17(2), a spouse may unilaterally sever a joint tenancy into a tenancy in common but may not appropriate all the property or the entire proceeds of sale. Creation of a joint account is not a completed gift. A completed gift occurs upon a withdrawal by a party of an amount more than the amount that party contributed to the account.

In a subsequent case, *Kobylski v. Hellstern (In re Estate of Kobylski)*, 178 Wis. 2d 158, 503 N.W.2d 369 (Ct. App. 1993), the court of appeals, in a significant footnote, corrected what it referred to as the impression left by *Lloyd* that an analysis of the character of an asset must be performed under section 766.63, the mixing statute. *Id.* at 173–74 n.7. Instead, said the court, analysis (described as a “character/gift/donative intent inquiry”) should be made under section 766.31(10), which expressly recognizes that a spouse may reclassify property by gift. If there is no gift, tracing may be done under section 766.63.

➤ **Comment.** Two inferences may be drawn from the *Kobylski* footnote discussed above: First, in the absence of donative intent, there is no automatic reclassification of property upon deposit of funds into a joint account. The funds could be reclassified by inability to trace, however. Second, if there is donative intent, there is a reclassification into marital property. This means that if individual property is deposited into a joint account with donative intent, a completed gift of one-half of the property occurs whether or not there are withdrawals.

For a case in which donative intent could not be proved, see *Gardner v. Gardner*, 190 Wis. 2d 217, 236–39, 527 N.W.2d 701 (Ct. App. 1994), a dissolution proceeding in which the court stated that the account was a temporary storage facility.

A lengthy and well-reasoned opinion with analysis limited to divorce cases is that of *Derr v. Derr*, 2005 WI App 63, 280 Wis. 2d 681, 696 N.W.2d 170. The opinion focuses on donative intent, saying:

We think it apparent that “character” terminology just adds a layer of haze to a topic that is already sufficiently complicated. Why not cut to the quick and use the term “donative intent” when talking about donative intent? No reason comes to mind and, therefore, in this opinion we will, when possible, avoid the terms “character” and “loss of character” and instead speak directly in terms of donative intent.

2005 WI App 63, ¶ 24, 280 Wis. 2d 681.

The court explained that, as a question of fact, donative intent is consistent with the general law of gifts, which requires an intent to give on the part of the donor. Some situations create a rebuttable presumption of donative intent, and the court identified the following four such situations:

1. Transferring nondivisible property to joint tenancy;
2. Depositing nondivisible property into a joint bank account;
3. Using nondivisible property to make purchases for the family; and

4. Using nondivisible property funds to make payments on a mortgage debt that was incurred to acquire jointly owned real estate. *Id.* ¶¶ 35–38.

The court drew a distinction between donative intent and *identity*, stating that donative intent reclassifies a part or all of an asset, depending on the scope of the donor's intent, while identity is a function of tracing. Assets can be of a mixed character without regard to donative intent although commingling of assets might suggest a donative intent. The court explained that tracing is used to describe the identity inquiry in marital property cases and that *Lloyd*, 280 Wis. 2d 681, could be read to suggest that the nature of the identity/tracing inquiry is the same in both marital property and divorce contexts. Noting that *Gardner v. Gardner*, 190 Wis. 2d 216, 527 N.W.2d 701 (Ct. App. 1994), on the other hand, may suggest the identity inquiry is somewhat different in the marital property context, the court limited its analysis to divorce cases. *Derr*, 2005 WI App 63, ¶ 24 n.7, 280 Wis. 2d 681.

After carefully defining the terms, the court applied a donative intent inquiry in *Derr*, a case in which the husband received an apartment building by gift from his parents, then subsequently used it as collateral to obtain a loan, the proceeds of which were used for general marital purposes. The issue was whether repayment of the loan from marital property cash converted some or all of the originally nondivisible inherited building into divisible property for purposes of divorce. The court said no, relying on the fact that the loan payments did not increase the net value of the building. Rather, the marriage received \$300,000 in loan proceeds equally matched by \$300,000 in debt. The court contrasted this situation with a situation in which a building's net value was increased with payments from marital property cash on a mortgage that finances acquisition or improvement of a building. Moreover, the court drew a distinction between simply putting the building at risk by using it as collateral and the situations listed above, such as using inheritance proceeds or other forms of nondivisible property to fund accounts for the benefit of the marriage. The former, they concluded, did not create a presumption of donative intent to give the building to the marriage, while the latter would have.

In *Steinmann v. Steinmann*, 2008 WI 43, 309 Wis. 2d 29, 749 N.W.2d 145, the Wisconsin Supreme Court considered a marital property agreement that classified certain assets as individual property of a party and also provided that upon a dissolution, assets classified as a party's

individual property would remain the property of that party. During the marriage certain of these individual property assets were titled into joint tenancy. The court noted that *Derr* involved the transmutation of nondivisible property acquired by gift or inheritance and that in *Steinmann* the nondivisible property at stake was created by marital property agreement. The court held that the principles of transmutation in *Derr* are not limited to nondivisible property acquired by gift or inheritance but apply to all types of nondivisible property, even that classified as individual property by a marital property agreement. The court then applied the basic principles of *Derr* and said that titling individual property into joint tenancy transmutes the property from nondivisible to divisible property if there is donative intent, and that the act of titling in joint tenancy raises a presumption of donative intent. Ultimately, the court found that the presumption was not rebutted even though the only testimony on the point came from the spouse denying that intent. The clear implication is that the reasoning of *Steinmann*, applied in a dissolution, will also apply in connection with marital property under the Act. Thus, titling individual property into a joint tenancy will transmute the property into marital property if there is donative intent, and it will be difficult to rebut the presumption that the mere act of titling in joint tenancy supplies that intent.

### **3. Marital Accounts [§ 2.264]**

The Act created section 705.01(4m), which establishes the right to create a new kind of account, a *marital account*, between parties who claim to be husband and wife. This is an account without the right of survivorship, because if the right of survivorship is added, the account is a joint account. Wis. Stat. § 705.01(4m), (4); *see supra* § 2.263. A marital account must be payable on request to either or both of the parties, and it must be designated as a marital account. Wis. Stat. § 705.01(4m). During both parties' lifetimes, the account belongs to them without regard to the proportion of their respective contributions to the sums on deposit or to the number of signatures required for payment. Wis. Stat. § 705.03(3).

If a husband and wife create a marital account, then upon the death of either of them and in the absence of a marital property agreement, after deducting payments and certifications made under section 404.405, the survivor owns 50% of the net sums on deposit, and the decedent's estate owns the other 50%. Wis. Stat. § 705.04(2m). If a marital account has



payable-on-death (P.O.D.) beneficiaries, then upon the death of either spouse, the surviving spouse owns 50% of the sums on deposit, and the P.O.D. beneficiaries named by the deceased spouse own the other 50%, subject to confirmation of the beneficiaries' rights under sections 865.201 and 867.046. Wis. Stat. § 705.06(1)(d).

A spouse who is a party to the account may withdraw from it, although with respect to the application of the funds, the other spouse may recover under section 766.70 if the conditions prescribed by section 766.70 are met. Wis. Stat. § 705.03(3). Aside from this latter remedy, a marital account functions like a joint account during the lifetime of both spouses and like a tenancy in common at death since there is no right of survivorship. Provisions protecting financial institutions are found at section 705.06. Language sufficient to create a marital account is set forth in section 705.02.

➤ **Query.** How is property classified after it is withdrawn from a marital account? Assume that a wife deposits \$1,000 of marital property into a marital account and withdraws it one day later. Is it marital property? The answer should be yes. The general rule is that all property of spouses is marital property unless classified otherwise. Wis. Stat. § 766.31(1). To allow one spouse to deposit funds in such an account and by later withdrawing it reclassify the funds is to allow unilateral reclassification of marital property. Neither the Act nor chapter 705 permits such reclassification.

➤ **Note.** Cases dealing with joint accounts, such as *Lloyd*, 170 Wis. 2d 240, and *Kobylski*, 178 Wis. 2d 158, *see supra* § 2.263, should not apply to marital accounts. Marital accounts have an attribute of tenancies in common in that, at death, the decedent spouse may dispose of only one-half of the account.

In cases in which there is more than one P.O.D. beneficiary and one of them predeceases a decedent spouse, the 50% interest owned by the deceased spouse passes to the surviving P.O.D. beneficiaries without regard to claims of the issue of the predeceasing P.O.D. beneficiary. Wis. Stat. § 705.06(1)(c). If all P.O.D. beneficiaries predecease the deceased spouse, 50% of the sums in the account are payable to the surviving spouse and the other 50% to the estate of the deceased spouse without regard to claims of the issue of a predeceasing P.O.D. beneficiary. *Id.*

## **XV. Federal Preemption [§ 2.265]**

### **A. In General [§ 2.266]**

Federal laws governing ownership of certain assets may preempt state law. The Supremacy Clause—Article VI, Clause 2 of the U.S. Constitution—is invoked when state and federal law conflict, and application of state law would frustrate the objectives of the federal program. *See McCarty v. McCarty*, 453 U.S. 210, 218 (1981). Such conflict occurs with certain retirement plans, as discussed in sections 2.211–.217, *supra*.

A surviving spouse has no claim under state community property laws for a portion of a National Service Life Insurance policy (a type of policy previously available to certain military-service personnel and qualified veterans). *See Wissner v. Wissner*, 338 U.S. 655 (1950). Similarly, Social Security benefits are not subject to state marital and community property laws. *See Luna v. Luna*, 608 P.2d 57 (Ariz. Ct. App. 1980); *Hillerman v. Hillerman*, 167 Cal. Rptr. 240 (Ct. App. 1980). Also, one authority states that although the separate or community property character of ownership of U.S. savings bonds is determined by state law, the extent of the spouses' dispositive power over the bonds is controlled by two U.S. Supreme Court decisions under the Supremacy Clause. *See McClanahan*, *supra* § 2.4, at 371; *see also Yiatchos v. Yiatchos*, 376 U.S. 306 (1964); *Free v. Bland*, 369 U.S. 663 (1962).

### **B. Copyrights and Patents [§ 2.267]**

#### **1. In General [§ 2.268]**

Federal preemption issues arise in connection with a spouse's rights under state marital (or community) property law in copyrights and patents obtained by the other spouse. The U.S. Constitution provides that to promote the progress of science and useful arts, authors and inventors should have the exclusive right to their respective writings and discoveries for a limited period of time. U.S. Const. art. I, § 8, cl. 8.

## 2. Copyrights [§ 2.269]

The Copyright Act of 1976, 17 U.S.C. §§ 101–914, is a federal statute providing protection in the copyright area to any creation expressed in tangible form. It was not until 1987 that a court dealt with the relationship between the federal law of copyright, particularly the Copyright Act, and the state law of community property.

*Worth v. Worth*, 241 Cal. Rptr. 135 (Ct. App. 1987), concerned a husband who wrote and published several books, including two books on trivia. In a 1982 divorce decree, the spouses agreed to divide the royalties from those books equally. In 1984, the ex-husband filed an action in federal court against the producers of the board game “Trivial Pursuit,” alleging copyright infringement. Thereafter, the ex-wife sought an order declaring that she was entitled to one-half of any proceeds derived from the lawsuit. The ex-husband resisted the wife’s claim on the theory that under the Copyright Act, a protected work “vests initially in the author or authors of the work,” 17 U.S.C. § 201(a), and thus belonged only to the author. He argued that this rule is mandated by federal law and preempts all state law to the contrary. The court disagreed.

First, the court noted that under California law any artistic work created during marriage constitutes a community property asset and that, if an artistic work is a community property asset, it must follow that the copyright itself obtains the same status. *Worth*, 241 Cal. Rptr. at 136–37. The court referred to 17 U.S.C. § 201(d)(1), which provides for the transfer of a copyright by contract “or by operation of law.” The court concluded that although the copyright vested initially in the ex-husband, the copyright was then automatically transferred to both spouses by operation of California law. *Id.* at 137. Thus, there was no irreconcilable conflict between state and federal law that would compel a conclusion that state law was preempted.

The Fifth Circuit Court of Appeals further developed the law in this area in *Rodrique v. Rodrique*, 218 F.3d 432 (5th Cir. 2000). The district court, 55 F. Supp. 2d 534 (E.D. La. 1999), had held that division of a copyright under state law interferes with federal policy and disagreed with the decision in *Worth* that half ownership in the copyright could be transferred by operation of a state community property law to the non-author-spouse. The district court suggested a possible solution, however; the author-spouse could retain and exercise sole management and control

of the copyright, but state law could transfer or divide the right to receive royalties. The district court declined to adopt that approach, because it felt congressional action was needed.

The Fifth Circuit Court of Appeals adopted the solution suggested by the district court, but disagreed that further legislation was needed on the point and therefore, reversed. Thus, the author-spouse retains management and control over the copyright, but the economic benefits belong to the community while it exists. In a footnote, the court said it was cognizant of the *Worth* court's transfer approach, i.e. its holding that a copyright vests initially in the author spouse but is then automatically transferred by operation of state community property law to the community. The court of appeals said:

Our approach is consistent yet analytically distinct; the author-spouse alone (at the time of creation and at all times thereafter, absent voluntary transfer of the copyright) is vested with the § 106 exclusive “fundamental rights”; those rights are never automatically transferred to the community. The *fruits* of the copyright, nevertheless, are community property at the “very instant” they are acquired.

218 F.3d at 438 n.26. The exclusive fundamental rights referred to above include reproduction adaptation, publication, performance and display.

### **3. Patents [§ 2.270]**

The analysis of how federal preemption affects copyrights may also be relevant to patents, but no cases have been found as of this writing.

## **XVI. Miscellaneous Property Interests [§ 2.271]**

### **A. Equitable Interests [§ 2.272]**

The definition of *property* in section 766.01(15) includes equitable interests vested or contingent. Thus, whether a contingent interest may ripen into possession is a matter of valuation. Is it necessary to classify a spouse's equitable interests in a trust created by a third person for that spouse's benefit? Any equitable interest that a spouse receives from a third person is a gift to that spouse from a third person and is, therefore,

the donee-spouse's individual property if it is received during marriage and after the determination date. Wis. Stat. § 766.31(7)(a); *see supra* § 2.8 (statutory definition of during marriage). A distribution of principal or income from the trust created by the third person is also that spouse's individual property. Wis. Stat. § 766.31(7)(a).

## **B. Contract Rights [§ 2.273]**

### **1. Private Annuities [§ 2.274]**

The classification of a private annuity is potentially complex. Typically, a private annuity is an arrangement whereby an individual transfers property to an individual, a corporation, or another entity not in the business of selling annuities in exchange for the transferee's promise to make periodic payments to the transferor at fixed amounts for the rest of the transferor's life. Private annuities are generally acquired in exchange for appreciated property that is usually a capital asset. If the annuity is measured by the transferor's life, payments may cease at the transferor's death, whether the transferor dies before, on, or after the date established as his or her normal life expectancy.

Often, annuities consist of three elements: (1) a return of capital; (2) a return for the appreciation on the item transferred; and (3) an income element. The taxation of private annuities is a complex subject and often involves prorating annuity payments between adjusted basis in the property, capital gain, and ordinary income. For a discussion of the taxation of private annuities, see John A. Warnick, *Private Annuities*, Tax Mgmt. (BNA) 805 (1994).

If marital property is exchanged for the annuity, the entire annuity obligation and the payments received are marital property. If, for example, the annuity is for a term certain and the transferor dies during the term and is survived by his or her spouse, one-half of the unpaid obligation is owned by the surviving spouse as that spouse's interest in former marital property.

If, however, individual or predetermination date property is transferred in exchange for the annuity, the return of capital is individual or predetermination date property. The appreciation is individual or predetermination date property, depending on the source of the appreciation. *See supra* §§ 2.90–.95. In the absence of a unilateral

statement, marital property agreement, or court decree to the contrary, the income is marital property to the extent it is earned or accrued during marriage and after the determination date. *See supra* § 2.8 (statutory definition of during marriage).

The more complex question is whether each element should be prorated as each payment is made. This is particularly relevant if the annuitant dies at an age younger than that considered to be his or her normal life expectancy. A court might follow the income tax analysis of annuities, prorate the elements of an annuity payment as received, and classify the elements according to that analysis. Whether classification should be based on an income tax analysis can be debated. The tax law allocates a portion of each annuity payment to ordinary income to minimize deferral of income for tax purposes. As an economic matter, it is arguable that each payment should be considered first a return of capital followed by a payment for the element of appreciation followed by income. Under the latter analysis, if the transferor died before receiving value equal to the fair market value of individual property transferred but after receiving an amount in excess of his or her original cost, no income would have been received; the return of capital would be individual property, and the payment received for the appreciation would be marital or nonmarital property, depending on the source of the appreciation. On the other hand, the income tax analysis has merit because it protects the other spouse's marital property interest in the income, an interest that the transferor puts at risk under an economic analysis if the annuity is based on life expectancy. As for the classification of the asset acquired by the purchaser, see section 3.25, *infra*.

## **2. Installment Obligations [§ 2.275]**

Installment obligations should be contrasted with annuities, *see supra* § 2.274. Installment obligations are usually for a fixed term and are payable regardless of the transferor's death. Installment obligations often consist of three elements: a return of capital; appreciation; and income, if a capital asset is involved.

If the asset sold is marital property, the entire obligation and all payments received are marital property.

If the asset sold is nonmarital property, the consideration attributable to the return of capital is nonmarital property. The consideration attributable to appreciation is nonmarital property or marital property, depending on the source of the appreciation. *See supra* §§ 2.90–.95. In the absence of a unilateral statement, marital property agreement, or court decree to the contrary, the income is marital property only to the extent it is earned or accrued during marriage and after the determination date. *See supra* § 2.8 (statutory definition of during marriage).

➤ **Query.** Assume that the transferor dies during the installment term. Must each payment be prorated among the three elements, or should the installments be treated first as a return of capital, then appreciation, and finally income? The three elements should be prorated pursuant to the terms of the contract with the result that some portion of each payment is attributable to interest income.

### 3. Land Contracts [§ 2.276]

Classification issues may arise in connection with land contracts, particularly in situations in which the vendee spouse has an equitable interest and the marriage terminates before all payments are completed under the land contract and before title to the real estate involved is conveyed to the vendee spouse. It is likely that a “buying-in” approach will be adopted in connection with land contracts under the Act since that approach is often used in connection with properties purchased subject to a mortgage. *See infra* § 3.25. Under the analysis in connection with properties subject to a mortgage, the equity in the contract is classified by tracing, if possible, to the classification of the assets used to make the purchase. If tracing is not possible, the equity is marital property under the presumption favorable to marital property. *See Wis. Stat. § 766.31(2)*. If, for example, a purchaser dies with amounts as yet unpaid for the property, the equity is classified as stated, and presumably the amounts paid by the successor in interest to the property are credited to that successor’s account and classified in accordance with the classification of the property used by the successor in interest. It is likely that a similar analysis will be followed for property purchased under a land contract, even though title is not conveyed until all installments have been fully paid. For different approaches, see section 3.31, *infra*.

#### **4. Covenant Not to Compete [§ 2.277]**

Payments under a covenant not to compete may well be analyzed as income replacements so that to the extent they replace income lost during marriage and after the determination date they are marital property, and to the extent they replace income during other periods, they are nonmarital property. However, a Washington case dealt with a covenant in connection with stock acquired by a spouse before marriage but sold during marriage. The same selling spouse then increased his earnings through new employment. The payments under the covenant, even though made during marriage, were held to be that spouse's separate property. *In re Marriage of Gillespie*, 948 P.2d 1338 (Wash. Ct. App. 1997). A covenant that restricts earnings during marriage might be characterized differently.

### **XVII. Assets That Are Difficult to Classify [§ 2.278]**

#### **A. In General [§ 2.279]**

At dissolution, some rights may be divided that are not assets classified under the Act. For example, courts in many community property and common law states have considered whether professional degrees and licenses, along with the accompanying professional goodwill, are property rights, and, if so, how they are to be valued and divided at dissolution.

#### **B. Professional Degrees, Licenses, and Tenure [§ 2.280]**

Generally, cases involving professional degrees or licenses arise after a spouse has either provided support for the other spouse or run the household and raised the children while the other spouse obtained a degree. Some cases arise shortly after the other spouse obtains the degree, but they can also arise years later after the other spouse has become established in his or her profession. In the latter case, the value of a degree is often overlooked, and more attention is paid to the goodwill generated by the degree-earning spouse's business. *See McClanahan, supra* § 2.4, at 124 (Supp. 1989). A useful summary of the law on this point, with a synopsis of cases and an excellent bibliography, is available. *See id.* at 120–38. Most of the cases hold that degrees and



licenses are not property, with the courts trying to achieve equity by fashioning solutions on a case-by-case basis. *Id.*

In Wisconsin, *Haugan v. Haugan*, 117 Wis. 2d 200, 343 N.W.2d 796 (1984), involved a dissolution that occurred shortly after a husband obtained a medical degree while being supported by his wife. At dissolution, the couple had little property. Under these circumstances, the court said that the degree, in a sense, was the marriage's most significant asset. *Id.* at 207. Although the court never stated that the degree was property, it held that a compensatory award should be made to the wife so she could participate in the husband's enhanced earning capacity. Techniques for valuing the contribution are set forth in the opinion. *See id.* at 211–15.

In view of *Patterson v. Board of Regents*, 119 Wis. 2d 570, 581, 350 N.W.2d 612 (1984), which held that tenure is a property right requiring due process protection, cases may evolve in which tenure is considered an economic factor at dissolution.

➤ **Query.** At the death of a spouse who is a professional, his or her professional goodwill or value in connection with a degree terminates, of course. What if the other spouse dies first, however? Presumably, there is no property interest in a license or degree that may be disposed of at death by the predeceasing spouse.

### **C. Professional Goodwill [§ 2.281]**

The notion of professional goodwill as property is distinct from the notion of a license as property because goodwill is generated from an existing professional entity having assets and history. Some period of operation is needed to provide goodwill, but once that history exists, goodwill may be valued along with other assets, according to courts in other jurisdictions. *See McClanahan, supra* § 2.4, at 138–44 (Supp. 1989). In Wisconsin, however, at least one court refused either to assign value to professional goodwill or to treat it as a separate property interest, saying the goodwill could not be sold or transferred and was merely a promise of future earning capacity. *Holbrook v. Holbrook*, 103 Wis. 2d 327, 351, 309 N.W.2d 343 (Ct. App. 1981). *But see Hauge v. Hauge*, 145 Wis. 2d 600, 606, 427 N.W.2d 154 (Ct. App. 1988) (estopping denial of consideration of goodwill in valuation process after testimony was given on goodwill's value).

A subsequent Wisconsin case, *Lewis v. Lewis*, 113 Wis. 2d 172, 180, 336 N.W.2d 171 (Ct. App. 1983), held that a buy-sell agreement between partners that established a value for a withdrawing partner's interest, including an amount for professional goodwill, established a concrete method of liquidating value; thus, a circuit court could use the entire purchase amount as a guide in valuing the spouse's partnership interest.

Note that the nonparticipant spouse enjoys an interest in a professional corporation, although he or she may not engage or participate in management or control of that asset. *See* Wis. Stat. § 180.1911(1). However, the nonparticipant spouse may not invoke the add-a-name remedy in section 766.70(3). Wis. Stat. § 766.70(3)(b).

#### **D. Fame [§ 2.282]**

Can fame be considered an asset? For example, can the reputation of a rock star whose name may lead to endorsements be considered an asset? Apparently, no cases have considered this matter, but commentators have. *See* Reppy & Samuel, *supra* § 2.19, at 199, and articles cited therein.

### **XVIII. Reclassification of Property [§ 2.283]**

#### **A. By Agreement [§ 2.284]**

The comment to section 3 of UMPA indicates “early and emphatically” that analysis of the classification sections of UMPA should not begin before noting that spouses may create their own classification system by marital property agreement. *See* Wis. Stat. § 766.17(1) (section similar to UMPA section 3). It is “clearly intended” under UMPA that contractual variances be possible with respect to classification of spouses' property generally, including life insurance and deferred employment benefits, and with respect to marital dissolution and disposition at death. UMPA § 3 cmt. The classification systems that may be adopted are virtually unlimited. Thus, spouses, by marital property agreement, may treat all or certain of their assets as individual property, marital property, solely owned property as if unmarried, joint-tenancy property, or tenancy-in-common property; indeed, the spouses could adopt the property law system of another state, or that which

existed in Wisconsin before January 1, 1986. For more about marital property agreements, see chapter 7, *infra*.

## **B. By Gift [§ 2.285]**

### **1. In General [§ 2.286]**

Spouses may reclassify their property by gift. Wis. Stat. § 766.31(10). Thus, after the determination date, one spouse may make a gift of his or her interest in an item of marital or nonmarital property to the other spouse and, by doing so, reclassify the item to the donee spouse's individual property. *Id.* A spouse may also give an item of his or her individual or predetermination date property to himself or herself and his or her spouse as marital property or survivorship marital property.

If one spouse gives property to the other spouse and intends when the gift is made that the property be the donee spouse's individual property, the income from the property is the donee spouse's individual property unless the donor's contrary intent regarding the classification of income is established. *Id.*

➤ **Practice Tip.** Presumably, the burden of proving such contrary intent is on the donor spouse or persons claiming through the donor spouse. From a planning standpoint, it is desirable to clarify in writing the donor spouse's intent regarding such income when a gift is made.

➤ **Query.** Documentation of a donor spouse's intent to make a gift and the donee spouse's acceptance of the gift may be advisable. Neither section 766.31(10) nor any other provision of the Act defines the word *gift*. However, section 766.31(10) begins with the plural *spouses* ("Spouses may reclassify their property by gift...."). Does this wording imply that both spouses must participate in a reclassification by gift from one spouse to the other in some affirmative manner that goes beyond the requirements of a completed gift under general law applicable to gifts? General law applicable to gifts requires donative intent and delivery by the donor, as well as termination of the donor's dominion over the subject of the gift and transfer of dominion to the donee. *Giese v. Reist (In re Estate of*

*Reist*), 91 Wis. 2d 209, 218, 281 N.W.2d 86 (1979). Going beyond these requirements would presumably involve a written declaration of gift signed by both spouses with delivery of at least one original of the declaration to the donee spouse.

A close reading of section 766.31(10) does not support the notion that such additional participation is needed to complete the gift. Section 766.31(10) states that spouses may reclassify their property not only by gift and marital property agreement, but also by conveyance, written consent under section 766.61(3)(e) (concerning life insurance policies), or unilateral statement. The last two methods of reclassifying property may be unilateral and do not require participation by both spouses. Thus, the word “spouses” at the beginning of section 766.31(10) is simply used in reference to the property that either or both of the spouses may own and does not, of itself, impose a requirement of joint participation beyond that required by pre-Act law.

Nevertheless, the requirements of a completed gift between spouses should also be analyzed in light of the type of property interest involved and, if a marital property interest is involved, in light of which spouse, the donor spouse or the donee spouse, has management and control of the asset. *See infra* §§ 2.287–.288.

## **2. Nonmarital Property [§ 2.287]**

A spouse who owns individual property owns all interests in the property and has total management and control over it. *See supra* § 2.108. During marriage, a spouse’s predetermination date property is treated as if it were individual property, and the spouse who owns it has total management and control over it. *See supra* § 2.145. Consequently, a gift by one spouse of his or her interest in nonmarital property (either individual or predetermination date property) to the other spouse with the intent to reclassify the property as the donee’s individual property is no different from a gift by one spouse of his or her solely owned property to the other spouse under pre-Act law. Meeting the requirements of pre-Act law (that is, general rules applicable to gifts) completes the gift.

A more complex situation arises when one spouse wishes to reclassify by gift his or her individual or predetermination date property to the marital property of both spouses.

➤ **Example.** Assume that a spouse owning real estate as his or her individual property simply executes a new deed containing the words “as marital property” after his or her name, records the deed, and advises the donee spouse of the transfer, but retains possession of the deed. Assume that there is donative intent but that the other spouse does not join in the conveyance. Has a gift to the other spouse been completed? Arguably, the retention of management and control means there is no transfer of dominion.

Section 766.31(10) permits spouses to reclassify their real property by a conveyance (as defined in section 706.01(4)) signed by both spouses. (Section 766.31(10) also provides that spouses may reclassify a security as defined in section 705.21(11) by an instrument signed by both spouses that conveys an interest in the security.) Thus, spouses owning real estate as joint tenants or tenants in common may reconvey the property to themselves as marital property or survivorship marital property or as one spouse’s individual property. Also, if nonmarital property real estate is titled solely in one spouse’s name, that spouse may reclassify the real estate to both spouses’ marital property if the other spouse joins in the conveyance.

In the example posed above, however, only the titled spouse participated in the conveyance. Nonetheless, reclassification can be accomplished if all the elements of a gift are satisfied. Wis. Stat. Ann. § 766.31(10) Legis. Council Committee Notes—1987 Act 393 (West 2009). Presumably, all the elements of a gift are satisfied in the example even though the donor spouse retained management and control. Under the Act’s management and control system, the titled spouse manages and controls marital property; that result does not change even if both spouses participate in the conveyance described. Moreover, the deed itself confirmed a change in ownership interests. In the circumstances posed, a gift should occur to the extent required for a reclassification under section 766.31(10).

➤ **Practice Tip.** Until the above analysis is confirmed by a court or by act of the legislature, spouses may wish to use a conveyance or a marital property agreement to ensure that a reclassification has occurred.

### 3. Marital Property [§ 2.288]

Since a titled spouse acting alone may reclassify nonmarital property by gift to the other spouse, a spouse with sole title to an item of marital property should be able to reclassify his or her interest in the property to the other spouse's individual property. In this kind of case, delivery of the document of title may be essential to complete the gift. The donee need not participate in the transfer, however, other than to accept the gift and take dominion over it.

When dealing with an interest in marital property, lack of management and control may pose a problem.

➤ *Example.* Assume one spouse alone has title to an asset classified as marital property and the other spouse (the untitled spouse) wishes to give his or her interest in the marital property asset to the titled spouse. How does the spouse without management and control manifest donative intent and effect delivery of his or her interest in the asset that is already titled in the donee spouse's name? A gift of real estate requires a conveyance by the untitled spouse meeting the requirements of section 706.02; since a conveyance must be used, the titled spouse may wish to participate in the conveyance so as to meet the literal requirements of section 766.31(10). Such participation is arguably unnecessary because, even under a common law analysis, all the requisite elements are met: there is donative intent, and dominion and control are vested in the donee. That the donor never had control should be irrelevant. *See supra* § 2.286. In any event, it may be prudent for the donor spouse to document the gift by executing and delivering a deed of gift rather than to rely on an oral expression of gift.

In cases involving untitled assets, questions may arise about the intent to make a gift and to reclassify the property. For example, in *O'Neill v. O'Neill*, 600 S.W.2d 493 (Ky. Ct. App. 1980), a case involving the definition of marital property as that term is used at divorce in the common law state of Kentucky, a doctor purchased expensive jewelry with his salary and delivered possession of the jewelry to his wife. The trial court excluded these items from marital property susceptible to division at divorce. The appellate court reversed, indicating that the husband's salary was certainly marital property, the jewelry when purchased did not lose that status, and mere change of possession did not

affect the nature of the property. The court also noted that the husband had testified that he purchased the items as an investment, hoping the jewelry would appreciate in value and could ultimately be converted to cash when needed for the children's education. The court further noted that there was no agreement between the spouses that these items would be the wife's separate property.

In Washington, a community property state, a different result was reached in *Johnson v. Dar Denne*, 296 P. 1105 (Wash. 1931). There, a wife bought diamond rings, apparently using "proceeds from her efforts." The court found that the rings were the wife's separate property by gift from her husband. This finding was based on comparatively slight evidence, principally the husband's prior statement that he had given the rings to his wife. For a similar case and result under pre-Act law, see *Potts v. Garionis*, 127 Wis. 2d 47, 377 N.W.2d 204 (Ct. App. 1985).

Issues involving reclassification by gift may also arise with certain expenditures or a change of title, especially in dissolution proceedings. Wisconsin's Act does not create presumptions in the gift context. Some other community property states, however, have developed such presumptions, which should be examined with caution before they are applied in Wisconsin. In California, for example, a judicially created presumption stated that unless an agreement between the parties specified that the contributing party was to be reimbursed, a spouse who used his or her separate property for community purposes intended a gift to the community. *Epstein v. Epstein*, 592 P.2d 1165 (Cal. 1979) (citing *See v. See*, 415 P.2d 776 (Cal. 1966)). This presumption was criticized because donative intent appeared to be imputed unless the donor spouse could obtain the donee spouse's agreement that the expenditure was not a gift. See *Reppy & Samuel*, *supra* § 2.19, at 44–45. On January 1, 1984, section 4800.2 of the former California Civil Code (West Supp. 1990) (now Cal. Fam. Code § 2640) took effect and reversed the result in *Epstein*, to the extent that, in dissolution proceedings, a spouse's contribution of separate property to the acquisition of community property must be reimbursed unless the contributing spouse made a written waiver of reimbursement. See *Perkal v. Perkal*, 250 Cal. Rptr. 296 (Ct. App. 1988).

In some community property jurisdictions, there is a presumption of a gift to the community when one spouse expends separate funds to acquire property, reciting co-ownership with the other spouse. See, e.g.,

*Sommerfield v. Sommerfield*, 592 P.2d 771, 774 (Ariz. 1979). *But see Bowart v. Bowart*, 625 P.2d 920 (Ariz. Ct. App. 1980). It is questionable that this presumption will apply in Wisconsin. *See infra* § 3.39. Some Wisconsin courts, however, have held that using inherited property to acquire property as joint tenancy or changing title by gift of inherited property to joint tenancy results in a change in the character of the assets involved, thus subjecting the assets to division at dissolution. *See Bonnell v. Bonnell*, 117 Wis. 2d 241, 246–47, 344 N.W.2d 123 (1984); *Trattles v. Trattles*, 126 Wis. 2d 219, 226, 376 N.W.2d 379 (Ct. App. 1985); *Weiss v. Weiss*, 122 Wis. 2d 688, 694, 365 N.W.2d 608 (Ct. App. 1985); *see also Derr v. Derr*, 2005 WI App 63, 280 Wis. 2d 681, 696 N.W.2d 170; *supra* § 2.263.

Whether reclassification by gift is a concept relevant only to interspousal gifts, and not to gifts to third parties made by spouses acting together, may be a question of little practical significance. Whether a gift by spouses to a third party is viewed as a reclassification of property (the better view) or as a divestment by both spouses of all their property interests in the asset given, the result is the same: the third party owns the property free and clear of the donating spouses' property interests. If, during marriage, only one spouse with management and control makes a completed gift of an item of marital property to a third person, the gift is complete from the moment of transfer. Wis. Stat. § 766.51(4). The property is then owned by the third party, and the spouse who did not act together with the donating spouse in the transaction has various remedies, including the right to reclaim the property from the third party donee if the gift exceeds the dollar amounts set forth at section 766.53. Wis. Stat. § 766.70(6)(a); *see infra* §§ 4.41, 8.45. A spouse who does not act together with the donating spouse has various rights of recovery for gifts to third parties of assets classified as marital property completed at the death of a spouse and for gifts made in joint tenancy form. *See* Wis. Stat. § 766.70(6)(b), (c); *see also infra* § 8.45.

➤ **Query.** What happens if one spouse, in effect, gives marital property to both the other spouse and a third party? Assume, for example, that a wife with management and control and donative intent makes a completed gift of marital property real estate to her husband and her unmarried son as tenants in common of an undivided one-half interest each, and her husband acts together with her in the transaction. In such a case, the husband's marital property interest in the real estate is reclassified by section 766.31(10) to an undivided interest as a tenant in common and is his individual property. The



undivided one-half interest owned by the wife's son is his solely owned property (not individual property because the son is unmarried). Regarding trusts, see sections 2.98–.104, *supra*.

### **C. By Unilateral Statement [§ 2.289]**

Although section 766.31(10) uses the term *reclassify*, in fact a spouse may by unilateral statement *classify* as individual property income accruing from his or her nonmarital property after the effective date of the statement. Wis. Stat. § 766.59(1). For more detail, see sections 2.70–.82, *supra*.

### **D. By Written Consent [§ 2.290]**

The spouses may reclassify life insurance policies and property used to pay premiums on such policies, or both, by written consent under section 766.61(3)(e). Wis. Stat. § 766.31(10); *see supra* § 2.177. The spouses may not use written consents to reclassify other types of property. *See* 1985 Trailer Bill Supplemental Nontax Note to section 766.61(3)(e); *see also supra* § 2.119.

### **E. By Decree [§ 2.291]**

In connection with certain remedies available to a spouse under the Act, certain court decrees can reclassify property from one classification to another. *See supra* §§ 2.105, .119; *see also infra* § 8.31.

### **F. By Mixing When Tracing Is Impossible [§ 2.292]**

Property may be reclassified because of a spouse's inability to trace the property. If, for example, nonmarital property cash is so mixed with marital property cash that it later becomes impossible to trace the nonmarital component, the nonmarital property cash is reclassified as marital property cash. Wis. Stat. § 766.63(1); *see infra* § 3.15.

### **G. By Attempt to Create Joint Tenancy or Tenancy in Common [§ 2.293]**

An asset may be reclassified as marital property with or without survivorship. If, for example, after the determination date in connection with a nonmarital property asset, a document of title, instrument of transfer, or bill of sale expresses an intent to establish a joint tenancy or tenancy in common exclusively between spouses, the nonmarital property asset is reclassified as survivorship marital property or marital property, respectively, unless a marital property agreement provides for a different result. Wis. Stat. § 766.60(4)(b)1.a., b.; *see supra* §§ 2.257, .258.

### **H. By Acquisition of Homestead [§ 2.294]**

Nonmarital property assets used to acquire a homestead exclusively between spouses after the determination date are reclassified as survivorship marital property if no intent to the contrary is expressed on the instrument of transfer. Wis. Stat. § 766.605; *see supra* § 2.251.

### **I. By Placement of Assets in Joint Account [§ 2.295]**

Transferring nonmarital property funds into a spousal joint account governed by chapter 705 after the determination date may reclassify the funds as marital property. If the transfer occurs while spouses are married but before the determination date, the funds may be deferred marital property. For further discussion, see section 2.263, *supra*.

## Mixing and Tracing

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## I. Methods and Consequences of Mixed Property [§ 3.1]

### A. Mixed Property [§ 3.2]

#### 1. In General [§ 3.3]

The Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or Wisconsin Marital Property Act], presumes that all property of spouses is marital property. Wis. Stat. § 766.31(2). The Act permits a spouse to own individual property and predetermination date property, but it imposes the burden on the owner

spouse to establish that the property is not marital property. Wis. Stat. § 903.01. The comment to Section 4 of the Uniform Marital Property Act (UMPA), *reprinted infra* appendix A, the act upon which the Wisconsin Marital Property Act is based, states that the presumption that all property of spouses is marital property is a general presumption; when “there is adequate proof to overcome the general presumption, then the proof will prevail and classification will be otherwise.”<sup>1</sup>

To complement the general presumption of marital property classification, the Act contains two provisions relating to mixed property. These provisions state that property can become mixed in two ways. First, mixing marital property, e.g., cash or assets, “with property other than marital property reclassifies the other property to marital property unless the component of the mixed property which is not marital property can be traced.” Wis. Stat. § 766.63(1). For example, depositing both a spouse’s marital property wages and the proceeds from security transactions involving individual property into a single account at a financial institution results in mixing. Mixing also occurs when marital property wages are used to pay an individual obligation on a mortgage note secured by individual real estate.

The second way property can become mixed under the Act involves substantial labor of either spouse performed during marriage on property other than the marital property of either spouse. This creates marital property, because in Wisconsin the economic benefits of substantial appreciation resulting from substantial labor inure to the spouses as marital property. Wis. Stat. § 766.63(2). Thus, the

[a]pplication by one spouse of substantial labor, effort, inventiveness, physical or intellectual skill, creativity or managerial activity to either spouse’s property other than marital property creates marital property attributable to that application if both of the following apply:

- (a) Reasonable compensation is not received for the application.
- (b) Substantial appreciation of the property results from the application.

Wis. Stat. § 766.63(2).

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189. Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

The general presumption and the accompanying mixing rules cause all property of a married couple to become marital property absent proof to the contrary (such as segregated assets or accurate records) or a contrary classification by a marital property agreement. Marital property agreements are considered in chapter 7, *infra*.

The 1988 Trailer Bill, 1987 Wisconsin Act 393 [hereinafter 1988 Trailer Bill], included two new ways of creating mixed property, which were necessary because of the change in the Act's definition of "during marriage." This change means that the Act does not apply after one or both spouses change their domicile to a jurisdiction other than Wisconsin.

First, the Act provides that an insurance policy issued after the determination date, which designates the insured as the owner, is marital property regardless of the classification of the property used to pay premiums on the policy. Wis. Stat. § 766.61(3)(a)1. The 1988 Trailer Bill added a provision to the effect that if, following issuance of an insurance policy insuring the life of a spouse after the determination date, the insured or the insured's spouse is at any time not domiciled in Wisconsin, the ownership interest and proceeds of the policy become mixed property. Wis. Stat. § 766.61(3)(c)2. The individual property component of the ownership interest and proceeds is determined by multiplying the entire interest by a fraction, the numerator of which is the period during marriage and after the determination date that the policy was in effect and the denominator of which is the entire period that the policy was in effect. *Id.*

Second, an interest in a deferred-employment-benefit plan may also become mixed property because of a change in domicile. A deferred employment benefit attributable to a spouse's employment after the determination date is mixed property if, after the determination date and during the period of employment, the employee spouse or the other spouse is at any time not domiciled in Wisconsin. Wis. Stat. § 766.62(1)(b). The marital property component of that mixed property is calculated by multiplying the entire benefit by a fraction, the numerator of which is the period of employment giving rise to the benefit that occurred after the determination date and during marriage and the denominator of which is the total period of employment. *Id.*

## 2. Mixing Deferred Marital Property [§ 3.4]

The Act's provisions regarding mixed property expressly apply only to marital property mixed with either (1) property having another classification or (2) the application of labor after the determination date by one spouse to property other than marital property of either spouse. Wis. Stat. § 766.63. The 1985 Trailer Bill, 1985 Wisconsin Act 37 [hereinafter 1985 Trailer Bill] added a provision that if the presumption that all property of spouses is marital property is overcome, the property is presumed to be deferred marital property. Wis. Stat. § 861.02(2). For example, if a spouse dies in 2010 owning 100 shares of XYZ, the presumption that the XYZ shares are marital property can be overcome if the stock certificate is dated before the determination date, but the property is then presumed to be deferred marital property. In attempting to rebut this second presumption, do the mixed property rules apply?

In a situation in which property that would have been marital property (deferred marital property) is mixed with property that would have been individual property, is the mixed asset reclassified as deferred marital property unless the component that would have been individual property can be traced? What about labor applied by a spouse before the determination date to property that would have been individual property if acquired after the determination date; is any substantial appreciation resulting from that labor classified as deferred marital property?

Although the Act is silent on mixing involving deferred marital property, applying the mixing rules is logical and effectuates the intent of the Act and the presumption of deferred marital property. Thus, all the techniques discussed in this chapter for tracing individual property and predetermination date property components from marital property also apply in segregating individual property and predetermination date property that would have been individual property from predetermination date property that would have been marital property.

## **B. Reasons Spouses May Wish to Avoid Mixing Property and to Retain Individual and Predetermination Date Property Classifications [§ 3.5]**

### **1. In General [§ 3.6]**

Mixing individual and predetermination date property with marital property can reclassify the individual and predetermination date property to marital property. There are many reasons a spouse may wish to retain individual property and predetermination date property, both during the ongoing marriage and at its termination. Some of the significant reasons are discussed below.

### **2. During the Marriage [§ 3.7]**

1. Individual property (other than that reclassified by marital agreement) and predetermination date property are not subject to obligations—whether contract or tort—incurred by the other spouse, except obligations imposed by the doctrine of necessities. By contrast, marital property is subject to such obligations if the obligations are incurred in the interest of the marriage or the family. Wis. Stat. § 766.55(2)(b).
2. Gifts of individual property and predetermination date property to third persons are not restricted. Gifts of marital property are restricted as to amount unless the spouses act together in making the gift. Wis. Stat. § 766.53.
3. If one spouse is subject to a bankruptcy proceeding, the other spouse's individual property and predetermination date property is not part of the debtor's estate. All marital property is.
4. A spouse has no duty of “good faith” in dealing with his or her own individual property or predetermination date property. There is such an obligation in dealing with either marital property or nonmarital property of the other spouse. Wis. Stat. § 766.15.



5. Individual property and predetermination date property may be used as collateral to obtain funds for nonmarital purposes or to improve other individual property. If marital property is used to improve individual property, the mixing rules apply and the individual property may be reclassified. Wis. Stat. § 766.63. For example, suppose a spouse has inherited a building worth \$100,000 and wishes to make a \$50,000 addition to it while maintaining the classification as individual property. This is possible if other individual property is available to be used as collateral for a loan or sold, with the proceeds being used to pay for the addition. If part or all of the addition is paid for using marital property, however, the mixing rules apply.

### **3. At Termination of the Marriage [§ 3.8]**

1. Property received by gift or inheritance (which would be individual property) is not divided at dissolution of a marriage unless failure to do so would cause a hardship. Marital property and all other nonmarital property is subject to division. Wis. Stat. § 767.61.
2. A specific bequest of individual property to a third party transfers the entire asset. A specific bequest of marital property transfers only half the asset because the surviving spouse owns the other half; the beneficiary and surviving spouse are tenants in common. Wis. Stat. § 861.01(1)–(2).

On the other hand, there are reasons a spouse who holds individual and predetermination date property may wish to change the classification of such property to marital property. The spouse may want to obtain the general objectives of equality, obtain specific objectives such as permitting the other spouse to have greater access to credit, or obtain a full adjustment to the tax basis of an asset upon the death of the first spouse.

## **II. Comparison of the Act with UMPA [§ 3.9]**

The Wisconsin rules regarding mixed property contain one significant difference from UMPA. Wisconsin's Act provides that substantial uncompensated labor expended by one spouse on *either* spouse's property, other than marital property, creates marital property. Wis. Stat. § 766.63(2). By contrast, UMPA section 14 applies this rule only to

substantial uncompensated labor by one spouse on the *other* spouse's individual property. *See infra* § 3.44.

### III. Tracing Situations and Methods [§ 3.10]

#### A. General Rules about Tracing Property [§ 3.11]

##### 1. UMPA and Commentators [§ 3.12]

A spouse uses tracing to establish the classification of an asset. If tracing is not possible, the presumption of marital property determines the classification of the subsequently acquired assets. Tracing is used in two situations: first, in cases in which an asset that was individual or predetermination date property is not retained to classify the subsequently acquired asset; second, in cases in which individual or predetermination date property is mixed with marital property to determine the proportionate ownership.

The comment to section 14 of UMPA provides that “tracing [will] necessarily be done under the appropriate tracing rules of an adopting state.” The comment states that these rules will build on the already existing solutions in probate and dissolution proceedings. For a summary of the procedures in the other community property jurisdictions, the comment cites W.S. McClanahan, *Community Property Law in the United States* §§ 6:7, 6:8 (1982); and William A. Reppy, Jr. and Cynthia A. Samuel, *Community Property in the United States* 113–300 (2d ed. 1982). For further discussion of tracing rules, the comment also cites Uniform Commercial Code section 9-306 (1962) (Wis. Stat. § 409.306).

The first step in tracing is to determine the particular property's classification at a particular point in time, such as at the date of marriage, date of inheritance, or date of acquisition. An asset may be marital property, individual property, predetermination date property, or mixed property in which the components can be identified. Note that the burden of proving that an asset is other than marital property is on the spouse asserting a different classification. To sustain the burden of proof in bankruptcy, the party claiming that an asset is not marital property must prove by the fair preponderance of the evidence that the nonexistence of the presumed fact is more probable than its existence. *Ludwig v. Geise (In re Geise)*, 132 B.R. 908 (Bankr. E.D. Wis. 1991).

When classifying an asset purchased over time, the funds used for the down payment must be classified, as well as the funds obtained from purchase-money debt. Reppy & Samuel, *supra*, at 91–97. If the debt is not classified, all the appreciation is allocated to the down payment, which is ordinarily smaller than the initial debt. This result is inequitable if the down payment and debt have different classifications.

For some purposes, it is necessary to subdivide the Act's property classifications. For example, in a divorce property division, only property acquired by gift and inheritance is excluded from division. This is narrower than the category of individual property, because individual property includes additional property, such as property owned by a spouse before marriage. As another example, predetermination date property that would have been marital property if acquired after the determination date is subject to the deferred marital property elections at death. Wis. Stat. §§ 861.02–.03. However, deferred marital property rules do not apply to predetermination date property that would have been individual property. Consequently, a spouse may want to separately trace the two types of predetermination date property and the various components of individual property.

Section 766.63 expressly provides that if property is mixed, the property is entirely reclassified to marital property if the nonmarital property component cannot be traced. If the components of the mixed property *can* be traced, does the spouse's contribution of marital property funds result in the spouse having an ownership interest in the asset or only a right to reimbursement of the amount contributed? If a spouse contributes substantial labor, does an ownership interest result or only a right to reasonable compensation for the services rendered? The question is relevant both for asset mixing and labor mixing. For example, if a spouse acquires a residence before marriage and makes mortgage payments and real estate tax payments from earned income during marriage, is part of the residence marital property? As a second example, if a spouse uses his or her labor to build an addition to an inherited cottage, does the cottage become partly marital property?

There are two theories for dealing with this issue:

[T]he two theories diverge when it comes to the valuation of the community's claim against separately owned stock that has appreciated by virtue of a spouse's time and effort. The "reimbursement" theory provides that the stock, as it appreciates, remains the separate property of the owner

spouse. Under this theory, the community is entitled to reimbursement for the reasonable value of the time and effort of both or either of the spouses which contributed to the increase in value of the stock. The “community ownership” theory, on the other hand, holds that any increase in the value of the stock as a result of the time and effort of the owner spouse becomes community property.

*Jensen v. Jensen*, 665 S.W.2d 107, 109 (Tex. 1984). Although a community property state may prefer one theory, all the community property states besides Wisconsin use both. See Reppy & Samuel, *supra*, at 80–82. Thus, a state may apply the ownership theory for some assets and the reimbursement theory for other assets.

The question is which alternative, if any, is favored in Wisconsin. The Act indicates a preference for having the marital component in mixed property be an ownership interest. This conclusion is not stated directly in the Act, but may be inferred from certain provisions in the Act and is consistent with the usual preference in other community property jurisdictions. Reppy & Samuel, *supra*, at 77–111. For instance, section 766.63(1) uses the term “component,” which implies that both parts have an equal interest. This is the result only if the interests are ownership interests. The statute further states that if tracing is impossible, a reclassification occurs. A reclassification is a change in ownership interest. *Id.* Section 766.63(2), dealing with a spouse’s labor in connection with either spouse’s property other than marital property, states that such labor creates marital property. In addition, when marital property is used to reduce a debt, this is defined as “acquiring” property. Wis. Stat. § 766.01(1). Finally, the conclusion that the marital component is an ownership interest is also consistent with the comment to section 14 of UMPA, which considers an “increased value resulting from payments on liens on property” as an example of a type of mixed property. The contribution of marital property is not a loan subject to reimbursement, with or without interest.

This section sets forth general rules about tracing property. When cash or assets of two classifications (i.e., marital property and nonmarital property) are used to acquire an asset, an issue arises as to the classification of the asset. There are two alternatives: (1) each spouse will obtain an ownership interest based on the classification of funds contributed to the acquisition; or (2) one spouse will own the asset as his or her nonmarital property and the other spouse will be entitled to reimbursement for the amount of marital property funds contributed

toward the acquisition. All other community property states use both the ownership and reimbursement techniques, and it is likely Wisconsin will also use both. Which alternative is applied depends on applicable law and the facts presented.

In considering whether Wisconsin courts would prefer one alternative, the Act appears to favor the creation of an ownership interest rather than a right of reimbursement. Professor William A. Reppy, Jr., has written an article about mixed property under the Act in which he questions whether the Act indicates a preference for the creation of an ownership interest instead of a right of reimbursement. *See* William A. Reppy, Jr., *Calculating the Spousal Interests in "Mixed" Property Cases Under Wisconsin's Marital Property Act*, Law. Marital Prop. F., Sept. 1990, at 17. Reppy concludes that section 766.63(1) is as likely to imply a reimbursement right as the creation of an ownership interest.

In most situations, the analysis in this book and in Reppy's article would compel the same conclusion. For instance, it appears that Reppy agrees that in an asset initially purchased with funds having different classifications, proportionate ownership interests are created. For example, if a residence is purchased for \$100,000, using \$20,000 of individual property funds and \$80,000 of marital property funds, the residence is classified 20% as individual property and 80% as marital property.

However, if an asset is purchased before marriage and is improved, or a debt is reduced using marital property funds, the analysis herein and the article may compel different conclusions.

For example, assume that a residence is purchased for \$100,000 before marriage, with \$20,000 used for the downpayment and a mortgage note executed for the remaining \$80,000. The \$80,000 mortgage note is satisfied using marital property funds. If an ownership interest is created, an 80% interest in the residence will be classified as marital property, including an 80% interest in any appreciation or depreciation in the value of the asset. If a right of reimbursement is created, the residence is entirely classified as individual property and the owner is obligated to reimburse the spouses' marital property for the \$80,000 of marital property funds used to reduce the indebtedness. There are no Wisconsin decisions under the Act dealing with this issue, although the analysis in this book suggests there is a preference for the creation of an ownership interest.

Reppy's article first reviews those portions of the Act that create an ownership interest by specific provision, section 766.63(2) (regarding the application of labor) and sections 766.61 and 766.62 (regarding interests in life insurance policies and deferred employment benefits). Reppy dismisses section 766.63(2) as a basis for finding a preference for an ownership interest in section 766.63(1) on the ground that it is one of the specific directives in the Act for an ownership interest and thus is not appropriate for such analogy.

Reppy next considers the analysis in this book favoring an ownership interest and addresses the definition of *acquiring* under section 766.01(1), which "includes reducing indebtedness on encumbered property." He sets forth examples and concludes that it is illogical to treat the satisfaction of a debt as creating an ownership interest because of this definition. The examples involve windfall appreciation in the value of property shortly after the satisfaction of a debt and, it is submitted, do not support a conclusion adverse to the creation of an ownership interest.

If the debt in Reppy's examples had been a mortgage obligation, the satisfaction of that obligation using funds having a different classification than the asset would create an ownership interest consistent with the classification of the funds used. If there was a subsequent windfall gain, all persons having an ownership interest would share proportionately in that gain. This is the holding of *Moore v. Moore*, 618 P.2d 208 (Cal. 1980), which is cited with approval in this book and by Reppy.

The decision in *Moore* also holds that the use of community property for the annual payment of real estate taxes, interest on the mortgage debt, and insurance premiums did not create an ownership interest in the community. Because Reppy cites the decision with approval, it appears that he also agrees with this part of the decision. *Moore* is presumably authority for the conclusion that payment of ordinary maintenance and repair expenses, including annually recurring real estate taxes, does not create an ownership interest. There may, however, be a right of reimbursement. Even though the real estate tax is a lien against the real estate from January 1, the removal of the lien apparently does not create an ownership interest. The Wisconsin Court of Appeals has also held that payment of real estate taxes does not create a divisible interest in the property. *Plachta v. Plachta*, 118 Wis. 2d 329, 348 N.W.2d 193 (Ct. App. 1984).

Reppy's examples involved a judgment lien and a real estate tax lien. The judgment lien was unrelated to the real estate and the real estate tax lien covered a number of delinquent years. The analysis in this book does not resolve whether satisfaction of these obligations creates an ownership interest. The definition of acquiring refers to "encumbered property." These liens appear to encumber the property; thus, the literal reading of the statute supports the view that the satisfaction of the obligation creates an ownership interest. On the other hand, to obtain an ownership interest by virtue of the failure to pay real estate taxes currently and not obtain an ownership interest when the tax is timely paid seems anomalous. Likewise, a judgment creditor's election to obtain satisfaction from a parcel of real estate instead of from other assets also does not seem to justify the creation of an ownership interest from one spouse's discharge of the obligation. A strong argument can be made that only encumbrances incurred by the consensual action of one or both spouses should cause changes in classification of an asset based on the satisfaction of a debt.

Whether the definition of acquiring shows a preference for creating an ownership interest does not require answering the issue raised by Reppy's examples. The definition clearly provides that the satisfaction of a mortgage obligation creates an ownership interest. This is specifically mentioned as "an important means of building assets" in the comment to UMPA section 1. Reppy's statement that the definition does not provide direction regarding purchase-money mortgages does not appear to be a logical conclusion based on his examples. The definition supports the conclusion that traced interests in property pursuant to section 766.63(1) are ownership interests.

Reppy does not respond to the use of the terms "component" and "reclassification" in section 766.63(1). A *component* is defined in the Act as the interest that must be traced if the entire asset is not to be classified as marital property. *Webster's Unabridged Dictionary* (Random House CD-ROM, 1999) defines *component* as "a constituent part." The definition is consistent only with an ownership interest. Reppy does not discuss the fact that a failure to trace causes a reclassification. A reclassification is a change of ownership. Significantly, the comment to UMPA section 14 also appears to prefer an ownership interest. See UMPA § 14.

Reppy next considers Wisconsin law before the Act. The cases cited do not support the proposition that Wisconsin has adopted a rule favoring

a claim for reimbursement rather than a buy-in remedy in its pre-Act dissolution and probate cases, being the type of cases referenced in the comment to UMPA section 14. The two cases cited by Professor Reppy for the proposition that a claim for reimbursement is preferred are neither dissolution nor probate cases and do not involve spouses.

*Gerndt v. Conradt*, 117 Wis. 15, 93 N.W. 804 (1903), concerned two unrelated parties who purchased a machine as equal tenants in common for \$150. Both parties contributed equally to the payment of the first \$100. The remaining \$50 was payable pursuant to the terms of a promissory note due three years after the date of purchase. When the note became due, for reasons not explained in the decision, only one of the parties paid the final \$50 purchase price, and that party retained possession of the machine. After the machine had been owned for 15 years, the owner in possession sold it for \$75. The assignee of the other owner brought an action to recover one-half of the sale price. The court held that the party who paid the additional amount had a right of contribution from his co-owner and that once that amount had been received, the co-owner was entitled to one-half of the sale price.

For unrelated parties, an ownership interest is established at the time of acquisition and does not change based on satisfaction of purchase-money debt in subsequent years. Each co-owner has a cause of action against the other if the obligation is not paid proportionately. Accordingly, this case is not analogous to marital property classification.

The second case cited by Reppy is *Scheiner v. Arnold*, 142 Wis. 564, 126 N.W. 17 (1910), in which a parcel of real estate had been held by the wife in her name. During the 15-year marriage, the husband used his funds to satisfy real estate taxes and a mortgage debt against the property. The wife died intestate, and because she had children from a prior marriage, the husband received no property either as curtesy or under the intestate laws then in effect. The property therefore passed to her heirs from her prior marriage. The husband subsequently acquired a one-fifth interest in the property from two of these heirs. The remaining heirs brought this action against the husband to partition the property and to obtain rent from him for his use of the property subsequent to the wife's death. The husband counterclaimed to recover the amounts he had paid on the mortgage and for real estate taxes during the marriage. The husband did not make this claim in the wife's probate proceeding.



The court held that when the husband used his funds to improve the wife's property, there was a presumption that gift had been made from the husband to the wife. Because there had been no agreement for repayment, the husband's counterclaim was dismissed. This result is not inconsistent with the analysis in this book. In all cases in which funds of one classification are used to improve an asset of another classification, the first question is whether a gift occurred. Only after it has been determined that no gift was intended can the contribution of those funds be found to change the classification of a portion of the asset.

Therefore, neither *Gerndt* nor *Scheiner* supports the conclusion that pre-Act Wisconsin cases favor finding a right to reimbursement rather than an ownership interest.

Reppy next cites *Lacey v. Lacey*, 61 Wis. 2d 604, 213 N.W.2d 80 (1973), as a case in which he asserts that a hybrid remedy was fashioned by the court. Before marriage, the wife purchased a parcel of real estate using funds borrowed from her father and from a third party. The wife made payments on this debt for the period before the marriage. After the marriage, payments were made for an additional 23 months from an account that included the spouses' pooled earnings. The property was then sold. In the divorce action, the issue was what portion of the proceeds should be allocated to the wife.

Citing the *Lacey* court's opinion that "the value of the wife's equity in the land contract as for [sic] the date of the marriage" was nondivisible and had to be confirmed to the wife, Reppy argues that a hybrid division of the asset was created. Reppy, *supra*, at 20 (quoting *Lacey*, 61 Wis. 2d at 608). But this is not a hybrid remedy; rather, it is one mandated by the Wisconsin divorce law then in effect, which provided that a spouse should receive all property owned by the spouse before marriage and all property acquired solely by the spouse's efforts. Thus, in all divorce cases it was first necessary to ascertain and value the property owned by the wife before the marriage. The case treats changes in the value of the property after the marriage differently because the divorce law so required. (Reppy notes the statutory difference in a footnote but states that the case still has precedential value when a spouse adds inherited property to a mixed asset. However, the Wisconsin Court of Appeals rejected reliance on the *Lacey* analysis in *Torgerson v. Torgerson*, 128 Wis. 2d 465, 470, 383 N.W.2d 506 (Ct. App. 1986).)

In his analysis of *Lacey*, Reppy also states that at the moment of marriage, the wife “lost the right to claim as her nondivisible property any further natural increase” in its value. Reppy, *supra*, at 20. This is not the holding. In fact, she was given the full value of the property through the time the debt was satisfied. The court held that the husband had a duty to support the wife and that his duty included a responsibility to provide a residence. The court found that the payments made from the pooled earnings during the term of the marriage were approximately equal to the amount the husband would have been required to pay as rent to satisfy that obligation if the wife had not already owned the property. Therefore, the court found that the payments could be considered as made from the wife’s property alone.

Reppy concludes his article by suggesting that the Arizona approach utilized in *Drahos v. Rens*, 717 P.2d 927 (Ariz. Ct. App. 1985), should be considered for adoption in Wisconsin. *Drahos* follows the decision in *Honnas v. Honnas*, 648 P.2d 1045 (Ariz. 1982), discussed in section 3.41, *infra*. To implement the *Honnas* decision, the Arizona court adopted the formula used in *Marsden v. Marsden*, 181 Cal. Rptr. 910 (Ct. App. 1982), which is also discussed in section 3.41, *infra*. Arizona does not recognize the creation of an ownership interest through satisfaction of debt as part of its community property law. At divorce, Arizona attempts to permit both spouses to share in the appreciation in the value of an asset when community property has been used to improve a spouse’s separate property by creating an equitable lien. Reppy indicates that this is a desirable method, because it leaves management and control with the titled spouse and limits creditors’ access to the asset.

In Wisconsin, management and control already follows title under the Act. Wis. Stat. § 766.51. A creditor’s ability to reach an asset may be different if no change in classification occurs by the payment. However, the spouse is likewise unable to obtain access to credit, which was one of the primary goals of the Act. The equitable lien approach can fairly treat the spouses at dissolution, but it does not give the nontitled spouse property to will at death and it does not give the nontitled spouse an ownership interest during the marriage that could be used to obtain access to credit and remedies. If the preferable policy is to allow both spouses to share in the appreciation or depreciation in the value of an asset based on the respective contributions of funds to the acquisition of that asset, then it appears that the creation of an ownership interest will more completely provide this result than the equitable lien approach utilized in Arizona.

Although Reppy also concludes that the analysis in this book “implicitly directs use of the ‘buy in’ approach in situations not specifically addressed by some other statutory provisions,” Reppy, *supra*, at 19, the analysis in this book concludes that there is a preference only. Section 3.29, *infra*, also analyzes specific instances in which reimbursement appears to be the appropriate remedy. When marital property funds are applied to acquire, improve, or maintain an asset, Wisconsin courts should adopt the view that the marital component created in the mixed property is generally an ownership interest; reimbursement of the amount contributed is appropriate in some cases involving mixed property, and in some de minimus or maintenance situations neither ownership nor reimbursement is appropriate.

## **2. Wisconsin Divorce Approach [§ 3.13]**

In determining the tracing rules previously applied in Wisconsin, the tracing of gifts and inherited property for purposes of property division in a divorce proceeding must be considered. Under the Wisconsin divorce statute, property received by inheritance or gift is normally excluded from property division. Wis. Stat. § 767.61. However, no reported decisions have specified the proof necessary to trace gifts and inherited assets. The courts have considered issues of proof, though, in connection with the appreciation of property received by inheritance or gift. Such natural appreciation is excluded from division, absent substantial labor contributing to the appreciation by the other spouse. *Plachta*, 118 Wis. 2d 329. No reported decision has analyzed what constitutes a substantial contribution. The courts have also considered whether the identity of a gift or inherited asset can be determined when its character has been transmuted. *Bonnell v. Bonnell*, 117 Wis. 2d 241, 344 N.W.2d 123 (1984); *Finley v. Finley*, 2002 WI App 144, 256 Wis. 2d 508; *Trattles v. Trattles*, 126 Wis. 2d 219, 376 N.W.2d 379 (Ct. App. 1985); *Weiss v. Weiss*, 122 Wis. 2d 688, 365 N.W.2d 608 (Ct. App. 1985). Putting gifts or inherited funds in joint tenancy has been held to cause a transmutation of character in which the property lost its status as inherited. *Id.* Likewise, the use of funds for household expenditures, household furnishings, and mortgage reduction on a jointly owned residence has been held to cause a loss of status. *Trattles*, 126 Wis. 2d 219. Even a temporary deposit in a joint account creates a rebuttable presumption of an intent that inherited funds be used for marital purposes and are thus transmuted to marital property. *Finley*, 2002 WI App 144, 256 Wis. 2d 508. These decisions do not clarify what tracing rules are

acceptable. However, the requirements appear strict when the original asset has been disposed of and a new asset has been acquired.

The requirements for establishing the identity of a gift or inherited asset were considered in *Brandt v. Brandt*, 145 Wis. 2d 394, 427 N.W.2d 126 (Ct. App. 1988). Income on gifts and inherited property is divisible. *Arneson v. Arneson*, 120 Wis. 2d 236, 355 N.W.2d 16 (Ct. App. 1984). In *Wierman v. Wierman*, 130 Wis. 2d 425, 387 N.W.2d 744 (1986), the court held that when a spouse receives an interest in a partnership by gift, the partnership's assets do not become divisible property if they are not managed by one of the spouses. The court did not distinguish between the partnership's ordinary income and its principal.

In *Lendman v. Lendman*, 157 Wis. 2d 606, 460 N.W.2d 781 (Ct. App. 1990), the court considered the divisibility of appreciation in the value of stock in a closely held business. The appreciation had occurred through the corporation's reduction of the indebtedness it had incurred when it purchased a business. The husband, who used inherited funds to acquire the stock in the corporation, was the principal employee of the corporation. The court held that the appreciation was not "purchased with funds acquired" by inheritance as required by the property division statute. The corporate income was generated through the husband's labors. This was considered to be income; following *Arneson*, appreciation paid for by income is divisible property. The *Lendman* court's analysis of income retained in a corporation is different from that both under the Act and utilized by courts in other jurisdictions. Wis. Stat. § 766.63(2); *see also infra* § 3.47.

In *Fowler v. Fowler*, 158 Wis. 2d 508, 463 N.W.2d 370 (Ct. App. 1990), the wife inherited stock in AT&T. As part of the company's divestiture, she received stock in regional telephone companies. She participated in dividend-reinvestment programs for those companies and thereby purchased additional stock. Her father also gave her cash gifts during the marriage that were deposited in either a joint checking account or in a savings account in the husband's name. Stock in her sole name was purchased using funds from those accounts.

The court held that the stock in the regional telephone companies was part of the property received by gift. It was not income on the AT&T stock, but rather substituted securities. On this basis, the court distinguished *Lendman*. The character remained the same because all the stock was titled in the wife's sole name. In addition, there was no actual

or constructive donative intent. The stock purchased pursuant to the dividend-reinvestment programs, however, was an asset purchased with income. Following *Arneson*, the court held that such stock is not property acquired by gift or inheritance. Finally, depositing the cash gifts in the joint checking account changed the character of that property, making it divisible. The amounts deposited in the savings account in the husband's sole name were commingled with funds representing the husband's wages and other earnings and the wife's salary. The circuit court's finding that these funds were so commingled as to lose their identity was sustained on appeal.

*Shreve v. Shreve*, No. 91-0635, 1991 WL 285884 (Wis. Ct. App. Nov. 5, 1991) (unpublished opinion not citable per section 809.23(3)), concerned a personal-injury settlement the husband had received during the marriage. The husband deposited the settlement into a joint bank account to be used for ordinary living expenses. At the same time he arranged to have a portion of his salary placed in retirement accounts. At the time of the divorce the husband claimed that the balance in the retirement accounts reflected the personal-injury settlement and should not be part of the divisible property. He also claimed that he had used the funds to obtain a tax advantage for the family. The court held that when the settlement funds were placed in the joint bank account and used for ordinary expenses, they were transmuted from separate property into divisible property. The funds in the retirement accounts were from the husband's income and not from the personal-injury settlement. Thus, the retirement account was divisible.

*Friebel v. Friebel*, 181 Wis. 2d 285, 510 N.W.2d 767 (Ct. App. 1993), involved distributions from two trusts created by the wife's father. The first trust required mandatory distribution of the net income to the wife and gave the trustee discretion to distribute the trust corpus to her. The trust corpus was scheduled to be distributed to the wife in specified shares upon her attaining certain ages, none of which occurred before the divorce. The wife also had the right to withdraw from the trust \$10,000 of each lifetime gift made by her father to the trust, but she never exercised this right and it lapsed. A capital gain had been realized in the trust and the taxation of that capital gain was reported on the parties' personal income tax returns. The capital gain was not, however, distributed to the wife.

The issue before the court was whether the net income distributed to the wife and the capital gain on which tax had been paid was income

subject to division in the divorce. The court held that income on property received by gift is only divisible when the party has the right to control the investment of the asset producing that income. In this case, the trustee had control over the investment of the trust assets. Thus, the court found that the funds received as a distribution of the net income were property received by gift and not subject to division. The court also found the capital gain was not divisible. Even if the gain had been distributed, it would have been property received by gift consistent with the court's analysis of the net income distributed from the trust. Thus, all property received as a distribution from a trust was property received by gift.

The father also created a second trust funded with cash and real estate. His wife and all his children were the beneficiaries. The trustee of the second trust had the discretion to pay income to the trust beneficiaries but never exercised this discretion. During the marriage, this trust terminated and the wife received a cash distribution.

After the wife received the distributions of net income, she created an investment account with a corporate trustee that remained in existence for four years. All the net income distributed from the trust was deposited in this account, as were the funds received upon termination of the second trust. During the four-year period, the investment account earned investment income of \$11,000, realized capital gains of \$4,000, and generated unrealized gains of \$4,000. The issue before the court was whether, by leaving the investment income in the account, the entire account had become so commingled as to make it divisible. Resolution depended on whether the wife had retained the identity of the funds as property received by gift. The court held that “[c]ommingling is not per se fatal to the exempt status of a gift; rather the inquiry is whether the gifted component can be valued.” *Id.* at 299. “All the assets deposited into [wife’s] account were gifts to her except readily determinable income generated by the account.” *Id.* This income, even if it includes the realized and unrealized capital gain, was only five percent of the value of the account. “We conclude that the entire account was not tainted by and so commingled with the five per cent of divisible property as to convert the remainder of the account into divisible property.” *Id.*

The wife conceded that all withdrawals from the account were of her property received by gift, and she agreed to divide the total income remaining in the account. This stipulation maximized the amount of divisible property. The court of appeals remanded the property division

to the circuit court with directions that the lower court resolve, among other issues, whether the realized and unrealized gains in the account were, in fact, income or instead appreciation resulting from general economic conditions such as inflation.

The treatment of the property distributed from the trust as property acquired by gift (regardless of whether it was income or capital gain of the trust) is consistent with the classification of such distributions under the Marital Property Act in section 766.31(7)(a).

*Derr v. Derr*, 2005 WI App 63, 280 Wis. 2d 681, 696 N.W.2d 170, is an attempt to clarify and reconcile the discussions in prior cases regarding identity and character. The court determined that tracing, not identity, was the correct term for the required inquiry. Similarly, the analysis that courts had sometimes termed *change in character* was changed to *donative intent*, which the court stated is directed at determining the owning party's *subjective* donative intent. "When an owning spouse acts in a manner that would normally evince an intent to gift property to the marriage, donative intent is presumed, subject to rebuttal by 'sufficient countervailing evidence.'" *Id.* ¶ 33. The court stated that its prior decisions had identified the following situations that create a rebuttable presumption of donative intent:

1. Transferring nondivisible property to joint tenancy;
2. Depositing nondivisible funds into a joint bank account;
3. Using nondivisible funds to make purchases for the family, such as expending the funds to acquire property, goods, or services that are normally used for the mutual benefit of the parties; and
4. Using nondivisible funds to make payments on a mortgage debt that was incurred to acquire jointly owned real estate.

Under the Wisconsin Marital Property Act, these enumerated actions are also likely to change presumptively individual property to marital property.

At the time of the parties' divorce in *Wright v Wright*, 2008 WI App 21, 307 Wis. 2d 156, 747 N.W.2d 690 (review denied), stock in Fall River Group, a closely held business, was titled in the name of the husband, Charles. He also held securities and a money market account at

a brokerage firm. He asserted during the divorce proceeding that each of these assets was gifted property and was not divisible. His wife, Linda, contended that Charles had not adequately established that the stock in the closely held business was gifted property, that the retained earnings of the business were divisible property, or that the appreciation in value of the business during the marriage resulted from Charles's efforts.

With respect to the brokerage account, Linda contended that the stock in the account could not reliably be traced to an original gifted asset and that the funds in the money market account had been transmuted through commingling into divisible property. With respect to each of these assets, the burden of proving the property was nondivisible lay with Charles, because he was the party arguing that the property was exempt. To satisfy that burden, he needed to establish the original gifted or inherited status of the property and that the property's character and identity had been preserved. A character inquiry examines whether the owner spouse intended to donate nondivisible property to the marriage, and an identity inquiry involves tracing the asset. With respect to the stock in Fall River Group, the corporate secretary testified that the shares owned by Charles were the same shares originally gifted to him by his father and grandmother before the marriage. The parties had stipulated that these shares had not changed since six years before the marriage took place, in 1984. The circuit court found the shares were gifted property. The circuit court also found that there was no evidence that Charles at any time evinced a donative intent to transfer the stock into the marital estate. Thus, the circuit court held, Charles satisfied his burden as to both the character and identity of the asset.

At this point, the burden of proof shifted to the nonowning spouse to establish that the property was divisible. Linda contended that there was no evidence introduced as to the value of the stock at the time the property was transferred to Charles or at the date of marriage and that without that knowledge it was necessary to treat the entire asset as divisible property. The circuit court held that this was really a question regarding whether the appreciation in the value of the stock during the marriage had resulted from the efforts of either spouse during the marriage. Only if the appreciation had resulted from effort by a spouse would the court need to know the beginning value so as to determine the amount of appreciation. Charles was a director of the business and was involved in the retention of the individual who ran the corporation's day-to-day operations. He stayed current on the company's financial results. The circuit court rejected this argument, finding that Charles was not



responsible for the appreciation in the company stock or the success of the company. The circuit court found that the appreciation resulted from the skills of the individual hired to run the day-to-day operations of the business. After 1982, Charles was not involved in running the business's day-to-day operations and he was not experienced in running a foundry. He had not actively managed the business or personally caused any appreciation in the stock's value.

Linda's final argument regarding the Falls River Group stock was that the retained earnings of the business were divisible. Insurance proceeds that replaced a business asset were the source of the retained earnings on the company's books. The circuit court found that when insurance proceeds arise from the loss of an asset they are not divisible, whereas when they compensate for a loss of income they are divisible. In this case, because the insurance proceeds were from the loss of an asset, the circuit court held that they were not divisible.

With respect to the money market account, Charles acknowledged that \$82,000 of divisible dividends were deposited in the account. In addition, testimony showed that additional cash was deposited in the account between 1998 and 2005, which Charles claimed was from distributions from two other gifted trusts. The amounts distributed, however, did not match up precisely to the amounts actually deposited in the money market fund. Charles testified that it was highly possible that marital funds were also deposited into the account. The circuit court held that the money market account maintained its gifted status, because there were no withdrawals from the account during the marriage, the \$82,000 of dividends could be taken out of the account and divided, and the deposit did not taint the entire account.

The court of appeals affirmed all of the circuit court's findings with respect to the Fall River Group stock. Because Charles had not been able to explain each of the money market deposits that took place during the marriage, the court of appeals held that he had not satisfied his burden to establish the character and identity of the gifted asset and thus the entire account was divisible property to be divided equally between the parties. The court of appeals did not explain why the original balance in the account at the time of marriage or in 1998 was not to be allocated exclusively to Charles, even though it had been agreed those amounts were gifted property.

### 3. Deposit of Nonmarital Property into a Joint Account [§ 3.14]

A question exists whether a deposit of nonmarital property funds into a joint account governed by section 705.02 changes the classification of the funds deposited to either marital property or survivorship marital property. The first inquiry is whether a joint account created under section 705.02 is a traditional joint tenancy. The Act is clear that if, after the determination date, spouses attempt to create a traditional joint tenancy exclusively between themselves, they do not, in fact, create a joint tenancy; rather, the property is classified as marital property and held as survivorship marital property. Wis. Stat. § 766.60(4)(b)1.a. The Wisconsin statute causing this result is not part of UMPA. The Note to the Wisconsin Act explains that the property is so classified for simplicity and because the classification arguably represents what most spouses will intend when they attempt to establish a joint tenancy after the Act is in effect. Nontax Provisions of the Marital Property Implementation Law: Original and Supplemental Explanatory Notes (1985 Wisconsin Act 37), Wisconsin Legislative Council Staff Information Memorandum 85-7, Part I, at 57 [hereinafter 1985 Trailer Bill Original Nontax Note to § xxx.xx or 1985 Trailer Bill Supplemental Nontax Note to § xxx.xx, as appropriate]. The Note further states that if the spouses wish to have the traditional incidents of joint tenancy, they may do so by marital property agreement. *Id.* The Note also explains that “the most significant difference between joint tenancy and survivorship marital property is that a joint tenant may unilaterally destroy the right of survivorship (for example, by conveying his or her interest in the joint tenancy),” while that is not true for survivorship marital property unless it is held in the “or” form. *Id.*

In determining whether a joint account is a traditional joint tenancy, one must consider the statutory characteristics of a joint tenancy and a joint account. The characteristics of a joint tenancy are set forth in section 700.17(2):

Each of 2 or more joint tenants has an equal interest in the whole property for the duration of the tenancy, irrespective of unequal contributions at its creation. On the death of one of 2 joint tenants, the survivor becomes the sole owner; on the death of one of 3 or more joint tenants, the survivors are joint tenants of the entire interest.

A joint tenant acting alone may not transfer more than his or her interest in the traditional joint tenancy.

The rule regarding lifetime ownership of a joint account is set forth in section 705.03(1), and the right of survivorship is set forth in section 705.04(1). The rules regarding lifetime ownership of a joint account are different from the rules that apply to a traditional joint tenancy. Section 705.03(1) provides that “the application of any sum withdrawn from a joint account by a party thereto shall not be subject to inquiry by any person, including any other party to the account and notwithstanding such other party’s minority or other disability,” except that the spouse of one of the parties may recover under section 766.70. Any party to a joint account may transfer the entire amount in that account. For this same reason, the creation of or addition to a traditional joint tenancy by one spouse is a gift to the cotenant, while a deposit to a joint account is not a gift until the nondepositing spouse withdraws funds from that account. But see *Lloyd v. Lloyd (In re Estate of Lloyd)*, 170 Wis. 2d 240, 487 N.W.2d 647 (Ct. App. 1992), discussed below.

The conclusion of this analysis is that a joint account under chapter 705 is not a traditional joint tenancy. Further support for this conclusion may be found in the 1992 Trailer Bill (1991 Wisconsin Act 301) [hereinafter 1992 Trailer Bill], which amended the statutory terminable opt-in and opt-out agreements. The agreements as originally enacted contained provisions on joint tenancies but did not specifically refer to joint accounts. It was therefore uncertain whether the agreements eliminated the survivorship aspect of a joint account. The 1992 Trailer Bill changed the statutory form of agreement to expressly provide that the agreements’ provisions do not affect the survivorship feature on a joint account under section 705.04(1). Wis. Stat. § 766.588(1)(d)2., (c)1.

➤ **Note.** Links to the 1992 Trailer Bill and other acts amending the Wisconsin Marital Property Act are available in appendix B, *infra*.

The second inquiry is whether the deposit of nonmarital property funds to a statutory joint account causes the funds to become marital property, even though the joint account is not a traditional joint tenancy and is therefore not subject to the mandatory survivorship marital property rule of section 766.60(4)(b)1.a. If the deposit reclassified the funds deposited, it would be consistent with the divorce decisions holding that the deposit of gifts or inherited funds into a joint account changes the character of the funds from gifts and inherited property into

divisible property. *Fowler v. Fowler*, 158 Wis. 2d 508, 463 N.W.2d 370 (Ct. App. 1990). But see *Zirngibl v. Zirngibl*, 165 Wis. 2d 130, 477 N.W.2d 637 (Ct. App. 1991). On the other hand, under section 766.63(1), the funds remain nonmarital if a spouse can trace the nonmarital property component in an account.

Two Wisconsin decisions have addressed this issue with inconclusive results. In *Lloyd*, 170 Wis. 2d 240, the husband periodically moved funds into and out of joint accounts in the name of the husband and wife. As a consequence, the wife had a right to withdraw the funds deposited into the joint accounts. The circuit court held that the deposit of predetermination date property funds into the joint accounts caused the funds to become classified as marital property. The circuit court did not apply tracing rules to determine whether the nonmarital component of the commingled account could be identified because, under its analysis, this tracing was not relevant.

The court of appeals cited this book for the applicable property law rules but used a character analysis in determining the classification of the funds in the joint accounts. The court used the rules applicable at divorce. The court held, “[t]he transfer of separately owned property into joint tenancy changes the character of the ownership interest in the entire property into marital property.” *Lloyd*, 170 Wis. 2d at 269. The court adopted the divorce standard and ruled that for a spouse to retain the ownership of an asset as nonmarital property, the asset must retain its character and identity as nonmarital property. Although the court discussed the rules regarding both joint accounts and tracing, it elected not to apply the rules. Instead, the court found that a change of character occurred when the deposit of funds occurred. As a result of this analysis, the court did not distinguish between traditional joint tenancies and chapter 705 joint accounts and did not consider section 766.60(4)(b)1.a. Likewise, the court did not consider this a mixing case.

The second decision is *Kobylski v. Hellstern (In re Estate of Kobylski)*, 178 Wis. 2d 158, 503 N.W.2d 369 (1993). Before the marriage, the wife held certificates of deposit (CDs) that were her nonmarital property. In 1986, one \$10,000 CD matured, and the wife deposited the proceeds into a joint bank account. In 1988, \$9,000 of that amount was used to purchase a vehicle titled in both names. The testimony of the surviving husband was that the \$9,000 was a loan to him, which he agreed to repay on demand if the wife should ask for it.

After the wife's death, her estate sought to recover the \$9,000 from the husband.

The court of appeals stated that the circuit court denied recovery "because the funds were drawn from a joint NOW account and the vehicle was titled in both spouses' names." *Id.* at 189. The court of appeals instead held that the wife's request for repayment was a condition of the obligation, and because the wife never requested repayment during her lifetime, the vitality of any claim expired with her.

In analyzing the case, the court of appeals cited this book for the applicable property law rules. The court did not analyze the significance of the fact that the automobile was titled in both names or the significance of the deposit of the predetermination date funds in the joint account. The court of appeals considered the court's analysis in *Lloyd* and stated the following:

In *Lloyd*, we also performed a character analysis. *Lloyd*, 170 Wis. 2d at 257–60, 487 N.W.2d at 653–54. Character addresses the manner in which the parties have chosen to title or treat the asset. When determining the character of an asset, the donative intent of the owner of the nonmarital property is an issue. *Id.* at 259, 487 N.W.2d at 654.

Because our character analysis in *Lloyd* was performed in the context of a mixing claim under sec. 766.63, Stats., our decision in *Lloyd* leaves the impression that a character analysis is conducted under that statute. Although it would not affect the result in *Lloyd*, we wish to undo that impression here. As we have already noted, a different statute, sec. 766.31(10), Stats., expressly recognizes that a spouse may reclassify individual property to marital property by gift. Therefore, any character/gift/donative intent inquiry under a character analysis is performed under sec. 766.31(10)—not sec. 766.63, the mixed property statute. Here, [the husband] makes no claim of gift by [the wife]. Thus, our analysis, like the probate court's, is limited to a tracing/identity analysis under sec. 766.63(1).

*Id.* at 173–74 n.7. It appears the correct analysis is that only tracing is required to maintain the classification of nonmarital funds deposited in a joint account. Normally, one must determine if a gift occurred. However, the deposit in a joint account of nonmarital funds is not a completed gift because the depositing spouse may withdraw the entire amount deposited. If no gift occurred, the issue in section 766.63, as stated by the court, is one of tracing.

## **B. Commingled Financial Accounts [§ 3.15]**

### **1. In General [§ 3.16]**

In trying to determine the source of an asset being classified, it is not uncommon to find that funds have passed through an account at a financial institution. Frequently, that account has received deposits of funds with different classifications, and expenditures have been made for different purposes. The courts in other community property states have developed methods for identifying and preserving the separate property (analogous to individual property in Wisconsin) in such accounts. Because of the Act's deferred marital property rules, unless classification is accomplished by marital property agreement, married persons residing in Wisconsin before the effective date must trace the sources of their existing assets to avoid subjecting them to election at the owning spouse's death. Wis. Stat. § 861.02(2)(a).

What are the rules for tracing an asset to determine its classification? Under the common law in Wisconsin, tracing was infrequent, and no clear rules developed. Tracing primarily occurred in divorce actions involving gifts and inherited assets. The decisions recognized that commingling inherited assets with other assets could result in a loss of the asset identity. *See, e.g., Finley*, 2002 WI App 144, 256 Wis. 2d 508; *Trattles*, 126 Wis. 2d 219; *Anstutz v. Anstutz*, 112 Wis. 2d 10, 331 N.W.2d 844 (Ct. App. 1983).

In developing new rules in Wisconsin for tracing assets to determine their classification, it will be helpful to analyze the decisions of the other community property states. It must be remembered, however, that many of the decisions have arisen in a divorce context in states that divide only community property. Wisconsin does not limit division at divorce to marital property. Thus, when Wisconsin courts consider the decisions in the other community property states, they may adopt less demanding standards to overcome the presumption of marital property.

## 2. Direct Tracing [§ 3.17]

### a. General Rules [§ 3.18]

Direct tracing is the most accurate method of tracing in community property states. The acquisition of each asset involves the payment of money, the exchange of another asset, or the incurrence of an obligation. In community property states, the source of the money or asset exchanged or the classification of the obligation incurred determines the classification of the asset acquired. Reppy & Samuel, *supra* § 3.12, at 114. To maintain individual property through direct tracing, it is necessary to have records of each transaction from the time an individual asset is acquired until the marriage terminates or a creditor raises the issue.

The general rule in other community property states is that if precise tracing becomes impossible at any point in an asset's history, the asset is transformed to community property. Given the Act's presumption that all property of spouses is marital property unless shown otherwise, the same rule appears to be true in Wisconsin. *See* Wis. Stat. § 766.31(1)–(2); *see also Wright*, 2008 WI App 2, 307 Wis. 2d 156.

With regard to commingled accounts, the other community property states have developed methods that satisfy the tracing requirement. For example, a ledger identifying each deposit and each expenditure will generally satisfy the tracing requirement in the other community property states. If one account is used for both individual and marital property deposits, the classification must appear in the ledger and each expense must be identified as pertaining to an individual or marital obligation. Reppy & Samuel, *supra* § 3.12, at 113–14.

In Wisconsin, unless a unilateral statement is executed, the spouse must not only record each deposit and each expenditure but must also maintain a record of income earned on individual property and predetermination date property and deal with marital property in the same manner as earned income. Wis. Stat. § 766.31(4). Direct tracing also may be accomplished by relying on agents or using an investment account or trust. Whether a particular direct-tracing technique has been established can be determined by asking whether the source of the amount used to acquire each asset can be directly ascertained. Reppy & Samuel, *supra* § 3.12, at 113–14.

Direct tracing constitutes actual proof of the classification from the initial receipt of the funds to the point at issue. Such proof will generally take the form of documents. Transactions involving deceased individuals should not be affected by the rule in sections 885.16 and 885.17 excluding certain evidence of such transactions. In Wisconsin, direct tracing should be acceptable in all situations. See *Fowler*, 158 Wis. 2d 508, a divorce case that involved the identity of funds that the wife had acquired by gift and that were then deposited in a savings account in the husband's sole name, which also contained funds from other sources. The court held the gifted funds were not traceable and lost their identity through commingling.

In *Ludwig v. Geise (In re Geise)*, 132 B.R. 908 (Bankr. E.D. Wis. 1991), the bankruptcy court used direct tracing to determine which assets in an individual retirement account (IRA) and an investment account were marital property and which assets were individual property. After tracing the dividends received and retained in each account, the court determined that the marital property assets were part of the bankruptcy estate.

The court also analyzed the balance in a personal checking account. The bankruptcy trustee successfully claimed that the balance in the spouse's checking account was marital property because the nondebtor spouse's salary had been deposited into the account during the marriage. It does not appear from the decision that any attempt was made to trace the various funds deposited in and expended from that account. The court found that the nonmarital funds were transmuted into marital property.

### **b. Illustrations [§ 3.19]**

Direct tracing is illustrated in *McKinley v. McKinley*, 496 S.W.2d 540 (Tex. 1973), in which the question was whether two savings certificates were community property. When the marriage took place, the husband had two savings accounts in his sole name. In one account, the only deposits that were made during the subsequent six-year term of the marriage consisted of the interest earned on the account balance. This interest increased the account from \$9,500 to \$10,453.81, at which time a withdrawal was made to create a \$10,400 savings certificate. The only prior withdrawal was in the exact amount of the interest previously credited to the account. The court held that the \$9,500 originally on



deposit was directly traced and was the separate property of the husband. The balance was community property.

The second certificate of deposit was in the amount of \$16,000. Of this, \$6,000 came from joint accounts consisting exclusively of community funds. The question related to the remaining \$10,000. As to that amount, the husband had a separate account of \$9,570.27 at the time of marriage. Between the date of the marriage and the date on which the certificate was taken out, numerous deposits and two withdrawals were made. Of the total \$7,740.34 deposited to the account, \$1,140.34 came from interest on the account balance and the remaining \$6,600 had an unknown source. Of the two withdrawals during the period, the first equaled the total interest earned to that date and the second was in the amount of \$4,985.91. After the \$10,000 withdrawal was made to purchase the certificate, the account balance was \$1,886.71. The court held that because there was no evidence to trace the separate funds initially on deposit in the account, any conclusion about the property's status would require speculation. The entire \$16,000 certificate was therefore held to be community property.

If, however, a positive balance had remained after subtracting from the account balance at the date of marriage (\$9,570.27, individual property) the withdrawal with the unknown purpose (\$4,985.91) and the subsequent deposits with an unknown source (i.e., \$6,600), the balance would have been sufficiently traced to the individual property of the decedent spouse. This result follows the approach used for the first account. *See Harris v. Ventura*, 582 S.W.2d 853 (Tex. Ct. App. 1979); *see also Snider v. Snider*, 613 S.W.2d 8 (Tex. Ct. App. 1981) (no writ).

The court of appeals used this type analysis in *Dins v. Dins*, No. 90-1588, 1991 WL 121043 (Wis. Ct. App. May 8, 1991) (unpublished opinion not citable per section 809.23(3)). The wife inherited funds from two relatives. She deposited the funds in a money-market account titled solely in her name. The husband claimed that by allowing the interest earned on the funds to remain in the account and by also depositing into the account the fee she received as personal representative of one of the estates, the wife had transmuted the inherited money to divisible property. He also claimed that other deposits of marital property funds in excess of \$18,000 were made to the account.

The circuit court held that the wife was entitled to be reimbursed for loans she had made to the family and that such reimbursement was the

basis for the other deposits to the account. The court also held that the wife had accounted for the source of every deposit to the account and given credit to the penny for all repayments made. The court held that the funds retained their inherited character. Because the title to the account was never changed and donative intent was never established, the court held that the funds in the account in the amount of the inheritance had been preserved as nondivisible property.

In *Lloyd*, 170 Wis. 2d 240, the husband had accounts in his sole name and also in joint tenancy with a third party on the determination date. During the marriage, the balance in a number of the accounts did not decline. The court of appeals found that in each of these accounts, the balance on deposit on the marriage date was traceable and remained the husband's nonmarital property.

### 3. Family-expense Doctrine [§ 3.20]

When direct tracing is impossible, the other community property states use the family-expense doctrine to permit some separate property to be identified and retained in a commingled account. The family-expense doctrine is predicated on a presumption that community funds are spent for family items, such as those for necessities and to satisfy support obligations, even though separate funds are also available. *Reppy & Samuel, supra* § 3.12, at 119. Thus, if a spouse proves that family expenses exceeded community income when an asset was acquired, the spouse establishes that the property was purchased with separate funds. *See v. See*, 415 P.2d 776 (Cal. 1966). It is not necessary to directly prove that community funds were used to satisfy the obligation. The conclusion arises from the presumption. *See Washington Community Property Deskbook* (Wash. State Bar Ass'n 3d ed. 2003) [hereinafter *Washington Deskbook*] (discussion of acceptance technique).

The circuit court must determine whether sufficient evidence has been introduced to satisfy the requirements of the family-expense doctrine. In this respect, the timing of the withdrawal in relation to the date of marriage or the date of deposit of individual funds is relevant. *Peterson v. Peterson*, 595 S.W.2d 889 (Tex. Ct. App. 1980) (writ ref'd n.r.e.); *In re Marriage of Cupp*, 730 P.2d 870 (Ariz. Ct. App. 1986).

The court summarized the family-expense doctrine in *Hicks v. Hicks*, 27 Cal. Rptr. 307 (1962):

When community expenses are paid from a bank account in which both community and separate funds have been deposited, it is presumed that they have been paid from the community funds therein ... . [I]f at the time of such payment, no community funds are on deposit and, for this reason, the payment is made from the separate funds therein, the latter will be reimbursed therefor from subsequent deposits of community funds. [I]n the event the amount of community expenses paid from the composite account exceeds the amount of community funds deposited therein, the balance of the money deposited, whether remaining in the account or transmuted to another form, is separate property.

*Id.* at 317. In *Hicks*, the family-expense doctrine was applied to a luxurious standard of living. The issue was whether the assets purchased through a bank account, as well as the remaining balance in the account, were the husband's separate property or whether, at divorce, the wife was entitled to one-half of the funds deposited in the account because the husband could not specifically account for the expenditure of the assets.

The parties were married for eight years, and the husband had accumulated a substantial amount of separate property before the marriage. During the marriage, the husband maintained a personal bank account, into which he deposited and from which he withdrew both community and separate funds. At the time of divorce, \$2,500 remained in that account. The testimony showed that during the term of the marriage, there were deposits into the account of \$557,124.71. Of that amount, \$546,545.93 could be traced. Of the traced amount, \$267,580.81 were deposits of separate property, and the remaining \$278,965.12 were deposits of community property. The difference between total deposits during the marriage and traceable amounts was \$10,578.78; because that amount had been acquired during marriage and the source could not be identified, it was presumed to be community property.

The court found there were withdrawals from the account for separate purposes in the total amount of \$172,931.80, leaving \$94,649.01 of deposits of separate funds in excess of withdrawals. The community expenditures for improving the community or joint-tenancy property, retiring community or joint-tenancy debts, and paying federal income taxes on the husband's salary and bonuses amounted to \$125,085.81.

The community deposits exceeded the community expenses by \$164,459.09.

The total family living expenses during the marriage were \$434,460, which substantially exceeded the community deposits available for their satisfaction. This amount was proved through an exhibit showing the payees of all checks drawn on the bank account during the marriage, along with a detailed analysis of the expenditures for one month of each year of the marriage. During this period, the wife had no separate source of income.

The court held that separate funds do not lose their character as such when commingled with community funds in a bank account, as long as the amount of separate funds can be ascertained. Whether funds deposited as separate funds continue to be on deposit when a withdrawal is made from the bank for the purpose of purchasing a specific property, and whether the intention is to withdraw only the separate funds from a commingled account are questions of fact. Evidence that establishes the availability of sufficient separate funds for separate purposes supports an inference that the owner of the funds used them for such purposes. *Id.* at 158.

Thus, applying the family-expense doctrine, the court in *Hicks* held that the assets acquired by the husband during marriage were purchased with his separate property and that the balance remaining in the account at the time of the marriage's dissolution was also the husband's separate property. The family expenses more than exhausted the community deposits that were unaccounted for.

The family-expense doctrine was also applied in *Mix v. Mix*, 536 P.2d 479 (Cal. 1975). In *Mix*, however, the schedule of funds and expenditures introduced in evidence showed only the sources of separate funds, the expenditures for separate property purposes, and the balance of separate property funds after the expenditures. The issue was whether real and personal property titled in only the wife's name was her separate property.

The wife was an attorney, and the husband was a musician and part-time teacher. At the time of the marriage, the wife owned several assets, including income-producing property, a residence, a life insurance policy, and separate bank accounts. After the marriage, the husband closed his separate account and the parties used a joint account into

which they deposited all their earnings as well as the wife's income from her separate property. Five years after they were married, the wife opened a separate account in her own name into which she deposited most of her income, both from her law practice and from her various investments. (In California, where the case arose, earned income is community property, while income on separate property is separate.)

The schedule introduced into evidence established that in all but one of the years the parties were married, separate property receipts exceeded separate property expenditures, leaving a balance of separate funds. In the one year in which a deficit did occur, it was not sufficient to exhaust the balance of separate funds carried forward from prior years. The husband contended that the schedule was flawed because the entries of receipts and expenditures of separate property were not tied to any specific bank account and thus showed merely the availability of separate funds, not the actual expenditure of separate funds for the enumerated separate purposes.

The court agreed that, by itself, the schedule was wholly inadequate to meet the test presented in *Hicks*. However, the court found the schedule was not the only evidence on this issue. The wife testified that the schedule was a true and accurate record of the receipts and expenditures that passed through various bank accounts and that it accurately corroborated her intention throughout the marriage to make the expenditures for separate property purposes from her separate property, notwithstanding the use of the balance of her separate property for general family expenses.

The appellate court found (as had the circuit court) that sufficient tracing had occurred to establish that all the real and personal property in the wife's name alone was her separate property. This result was reached even though the amount of family expenses was never established. The court relied on the corollary presumption that "[e]vidence establishing the availability of sufficient separate funds for separate purposes supports an inference that the owner thereof used such funds for such purposes." *Hicks*, 27 Cal. Rptr. 307 at 316; *see also See*, 415 P.2d 776.

*In re Marriage of Pearson-Maines*, 855 P.2d 1210 (1993), concerned the wife's ownership of a parcel of residential real property before the marriage. The property was destroyed by fire during the marriage, and the wife received an insurance reimbursement for the loss. After these

funds were received, the residential real estate was rebuilt. The wife maintained a detailed record of the expenditures made to rebuild the property. The insurance proceeds had been deposited into a bank account into which both spouses' earned income was deposited. The issue was whether the funds expended from that account to rebuild the property had been so commingled as to make tracing impossible, thereby converting the entire value of the residence to community property.

To maintain an asset as separate property, the funds must be both traced and identified. The court held that the insurance proceeds took the character of the property insured and, therefore, were the wife's separate property when initially received. "The presumption is that if there are both separate and community funds and there are sufficient separate funds from which the payments can be made, then the payments will be presumed made from such separate funds." *Id.* at 1214. The court held that the wife's records of the precise expenditures made for the construction of the new residence and her records regarding the other deposits and withdrawals from the account sufficiently traced the use of the insurance funds to have that portion of the property classified as her separate property.

The court noted that a different result would occur if the insurance proceeds had been used to purchase some asset unrelated to the wife's separate property. In that case, the community property presumption would apply and the separate nature of the new asset could not be established unless the community funds were shown to be dissipated. It is not clear why this would automatically be the result if the same detailed records were maintained.

The family-expense doctrine is most often used to trace funds having a different classification through commingled accounts. For example, assume the following checking account transactions:

		Balance
1. Deposit W's salary	4,000	
2. Deposit W's individual stock proceeds from sale of ABC	3,000	7,000
3. Check to gas company	100	6,900
4. Check for mortgage	1,000	5,900
5. Deposit W's dividend on individual security	200	6,100
6. Check to plumber	300	5,800
7. Check to cash	100	5,700
8. Deposit checking account interest	100	5,800
9. Check for real estate taxes	2,000	3,800
10. Check for charge card	500	3,300
11. Check for W's purchase of stock XYZ	2,800	500

Is the XYZ stock the wife's (W's) individual property or marital property? That depends on whether W can trace the purchase proceeds of XYZ to the proceeds received from the sale of ABC. Direct tracing is impossible because W did not record the source of funds for each transaction, but the family-expense doctrine can be applied.

The first step is to determine the extent of the individual property. If W has not executed a unilateral statement, the only deposit of individual property is the \$3,000 of sale proceeds from ABC. If W did execute a unilateral statement, then W's \$200 dividend and a portion of the checking account interest is also individual property. The account interest must be allocated between the interest attributable to marital property funds in the account and that attributable to individual property funds.

The next step is to consider the withdrawals from the account. Under the family-expense doctrine, the presumption is that marital property funds are spent for family items. The checks for the gas company bill, real estate taxes, plumber, and mortgage are family-expense items if incurred for residential real estate used by the family. However, if the expense is incurred for investment real estate, that property must be classified. For example, if the mortgage payment was made for a rental property that was the individual property of W, the part of the payment that was principal would be presumed made from nonmarital funds if those funds were available in the account because it would increase W's

equity. The interest portion would be presumed made from separate funds, if available, because it would be an expense in connection with the maintenance of individual property. The checks for the gas company, the plumber, and the real estate taxes would undergo similar treatment if they represent expenses incurred for W's individual property. The identification of the items purchased with the charge card is unknown, and there is no presumption based on the check's payee. To classify these withdrawals as family expenses, additional testimony or evidence must be introduced as to the use of the funds.

Assuming that no such evidence is introduced and that W did not execute a unilateral statement, the amount of individual property available to purchase XYZ is \$3,000 minus the \$600 withdrawals for cash and the charge card payment, less the expenses in connection with the real estate if it is W's individual property. Because W's funds remaining at the time of purchase of XYZ are less than the purchase price, W has only a pro rata ownership of XYZ stock. W's individual component, however, has been sufficiently identified to satisfy the mixing statute's tracing requirements. The same result would be reached by subtracting family expenses from marital property deposits.

The family-expense doctrine provides sufficient certainty for the Wisconsin courts to use it in classifying property. Moreover, the doctrine is equitable, and the courts could avoid having all expenditures required to maintain a luxurious lifestyle come from the marital property by limiting the expenditures that are permitted as expenditures of marital property. The limit could be set by the expenses included under the family-purpose doctrine, *see infra* chapter 5.

#### **4. Recapitulation of Community Income and Expense [§ 3.21]**

Some community property states extend the family-expense doctrine to permit commingled property to be sorted out through recapitulation of the total community income and expenses. Under this approach, if a spouse proves that total community expenses exceed community income, all acquisitions are separate property. The theory looks to the aggregate number of dollars rather than to the details of each transaction during the term of the marriage.



Reimbursement occurs automatically when recapitulation is used: if a community expense is in fact paid with separate funds because no community funds are available, the expense is charged to the community when the aggregate totals are determined. This result will occur even though the spouses never had an agreement regarding the reimbursement. *Reppy & Samuel, supra* § 3.12, at 119.

Idaho, Arizona, and New Mexico use the recapitulation method. In *Houska v. Houska*, 512 P.2d 1317 (Idaho 1973), the court determined the net income from all sources that would be community property and then deducted from it all the community living expenses to determine the community's share of commingled investments, including cash, livestock, crops, and farm vehicles. In *Moore v. Moore*, 379 P.2d 784 (N.M. 1963), the court approved an approach of analyzing the income of the community in each year and deducting amounts spent on community purposes and on the other spouse's separate property. *See also Porter v. Porter*, 195 P.2d 132 (Ariz. 1948); *Josephson v. Josephson*, 772 P.2d 1236 (Idaho Ct. App. 1989).

Not all jurisdictions accept the recapitulation method, however. For example, it was considered and rejected by the California Supreme Court in *See*, 415 P.2d 776. In that case, the husband received total wages in excess of \$1 million during marriage. He maintained two accounts from which expenditures were made and into which commingled community and separate property funds were deposited. Direct tracing was impossible because he had not maintained the necessary records. The court held that the husband could have maintained his separate property by not commingling community and separate funds. According to the court, once a spouse commingles assets, he or she assumes the burden of keeping records adequate to establish the part of the commingled aggregate that is separate property. Only when tracing is impossible through no fault of the spouse may recapitulation of the total community expenses and income throughout the marriage be used to establish the classification of the property.

The court in *See* explained why the family-expense doctrine was acceptable and recapitulation was not. Under the family-expense doctrine, a spouse may prove that all the community income was in fact exhausted by family expenses, and thus, that any assets that were purchased were purchased with separate funds. The recapitulation theory instead disrupts the community property system and transforms the interest of the non-wage-earning spouse into an inchoate expectancy, to

be realized only if at the termination of the marriage the community income during the marriage is found to have exceeded the community expenditures. The fact that a spouse uses his or her separate property to maintain a standard of living that cannot be maintained with community resources alone does not entitle that spouse to reimbursement from subsequently acquired community assets to make whole his or her separate property. Such reimbursement is permissible only if the spouses have an agreement between the parties to that effect.

Thus, in California, separate property is reduced to the extent it is used for family expenditures at a time when there is no remaining community property to satisfy the obligations. A subsequent deposit of community property provides no reimbursement absent an agreement between the spouses.

In Wisconsin, more liberal tracing rules may be adopted with regard to assets acquired and transactions that occurred before the determination date, because at the time of the transaction there is no reason for either spouse to maintain records that would permit direct tracing. Thus, even if recapitulation is rejected for transactions after the determination date, it may be approved for transactions before that date.

## **5. Maximum Marital Benefit [§ 3.22]**

If historical records are not available to determine the individual property component of a commingled account, it is still possible to establish some property as individual by limiting the marital component to the maximum benefit it could have realized. This theory assumes that all undocumented family expenses are satisfied from individual property even though they could properly be satisfied from marital property. A further assumption is that all the marital property is invested in the assets remaining at death or dissolution. The difference between the total value of the remaining assets and the value of the marital property component of those assets is individual property. This approach should be accepted in Wisconsin because all doubts are resolved in favor of a marital property classification.

One case in which a court used this maximum-marital-benefit approach is *Duncan v. United States*, 247 F.2d 845 (5th Cir. 1957). The decedent, a resident of Texas, owned a number of securities in his sole name, had a credit balance at a brokerage firm, and had a balance in an

account at a financial institution. His widow contended that this property was community property in which she was entitled to share. During the marriage the total community property available for investment was \$16,737.19, an amount that was ascertained from the decedent's income tax returns. The income was reduced for contributions and taxes shown on the returns, but no reduction was made for living expenses paid during the marriage, even though they were presumptively community disbursements. The assets at the husband's death had a value of \$81,688.84. The bank account included deposits of all earned income as well as the income from the decedent's separate property. The securities were purchased using funds from that account.

The court held that when the facts conclusively demonstrate that even if every cent of community funds was invested, the figure would still amount to only a fraction of the cost of the property acquired, then the presumption that all the couple's property is community property has no factual basis and is overcome. That does not necessarily mean, however, that all the property must be classified as separate property. The community is entitled to the property that was in fact purchased with the available community funds. The court held that the community funds available went ratably into each security purchased.

Under the pro rata ownership approach used in *Duncan*, investments that result in losses need not be attributed to the community. For example, suppose \$10,000 of community funds and \$10,000 of separate funds are available for investment and that a spouse invests \$5,000, all of which is subsequently lost. Under such circumstances, courts normally would not allocate any part of the investment to the community but would allocate it to the separate property and leave \$10,000 of community funds in existence. See, e.g., *Succession of Ferguson*, 84 So. 338 (La. 1920). See also the discussion of *Friebel v. Friebel*, 181 Wis. 2d 285, 510 N.W.2d 767 (Ct. App. 1993) at section 3.13, *supra*.

## **6. De Minimis Commingling [§ 3.23]**

Another approach used to segregate and retain individual property is to establish that the amount of marital property commingled with the individual property was insignificant. UMPA § 14 cmt. The comment states that courts should not permit a serious injustice to result from mixing a minimal amount of marital property with a substantial amount of other property. See *Washington Deskbook*, *supra* § 3.20 (approves de

minimis commingling rule); *see also* Reppy & Samuel, *supra* § 3.12, at 128 (“It has often been declared that when a small amount of community property becomes commingled with a large sum of separate funds, uncommingling by tracing being impossible, the total mass is separate property rather than community.”). There is no reason for Wisconsin to deviate from this view.

A Wisconsin court refused to employ equitable tracing techniques in a divorce case. In *Brandt v. Brandt*, 145 Wis. 2d 394, 427 N.W.2d 126 (Ct. App. 1988), the court of appeals was required to rule on whether certain assets acquired by inheritance could be identified at the time of divorce and, therefore, could not be included in the estate subject to division.

The couple was married in 1952. Over the course of the marriage, the parties had nearly 30 separate investment, savings, and checking accounts at several different institutions. In 1963, the wife received a substantial inheritance and placed it in an investment account in her name at a brokerage firm. She gave her husband a power of attorney that authorized him to manage the account. The proceeds from the account were used during the marriage for family purposes, gifts, reinvestment, and deposit to the parties’ various accounts. During the marriage, the husband received income from his employment and also received approximately \$100,000 by gift and inheritance. There were a number of deposits to the wife’s investment account from salaries, gifts, other inheritances, and the other joint and sole accounts. Funds regularly flowed into, out of, and back and forth among the accounts.

The issue before the court was whether the balance in the wife’s investment account was inherited property. Among other arguments raised by the wife to support her position that the balance constituted inherited assets was her claim that the mixing was de minimis. As such, she asserted that either the entire balance should be classified as inherited property because the mixing was minor or the value of the amount inherited should be allocated to her as inherited property. The brief submitted on behalf of the wife cited to this section of the book.

The court held that “[c]ommingling, in and of itself, is not necessarily fatal to the exempt status of a gifted or inherited asset. The critical inquiry is whether, despite the commingling, the inherited or gifted component of the asset can nonetheless be identified and valued.” *Brandt*, 145 Wis. 2d at 412. The court also held that while some portion

of the wife's investment account undoubtedly represented a part of her inheritance, it was impossible with any degree of certainty to identify or value that portion.

In a footnote, the court stated,

[a]s an alternative to her tracing argument, [the wife] advances several novel theories under which her inheritance might be preserved. These include a 'reimbursement' theory and a 'de minimis commingling' theory. Although these theories have been adopted in some jurisdictions, they run contrary to previous rulings of the Wisconsin appellate courts that failure to preserve the character and identity of exempt property renders such property [divisible].

*Id.* at 413 n.4. This implies that equitable tracing rules such as reimbursement and de minimis commingling are not appropriate in a divorce context and are not persuasive in a property law context. The court's conclusion appears to be a stronger statement than was necessary to resolve the case.

A bankruptcy court has considered whether the de minimis rule should be adopted in Wisconsin in some cases. In *Geise*, 132 B.R. 908, the wife owned a residence as her individual property. During the marriage but before the filing of the bankruptcy petition, she had paid down the \$40,900 mortgage note with \$260 of her marital property wages, leaving a balance of \$40,640.

The home appreciated in value by \$3,120 during the marriage. Counting the marital property funds to reduce the mortgage principal balance would have made .52% of that asset marital property and cause that portion of the appreciation in value to also be marital property. However, the court found the aggregate of these amounts to be a "trifling sum." Thus, the court found that the entire residence remained the wife's individual property. The court recognized that the *Brandt* decision had rejected the de minimis approach in a divorce context and cited with approval the analysis in the supplement to this book that the conclusion in *Brandt* was not persuasive in a property law context.

In *Friebel*, 181 Wis. 2d 285, the court dealt with the accumulation of income in an investment account held by a corporate trustee and in which all funds deposited to the account were gifts. The court did not expressly determine that the income earned on that account was de minimis. However, the court did conclude that the accumulated income was only

five percent of the total value of the account and that the classification of the entire account was not tainted by and so commingled with this accumulated income as to convert the remainder of the account into divisible property.

A good example of a case in which the court followed this position is *Bowart v. Bowart*, 625 P.2d 920 (Ariz. Ct. App. 1980). The parties were married for 10 years. The wife was a beneficiary of trust funds with an annual income of approximately \$250,000; the husband was a writer who received sporadic income. One issue was whether real estate owned by the wife before marriage was subject to a community property lien because community funds in the household account were used to fund improvements to the real property.

The court found that the funds in the household account were almost entirely from the wife's separate trust. The husband's meager and sporadic contributions to the account failed to render the entire household account community property. Moreover, the account did not become community property because the wife placed her separate funds in a joint checking account. No presumption arose that the wife had made a gift to her husband of one-half of the funds. The husband was authorized to write checks on the account, but the evidence disclosed that this was merely a matter of convenience and was not intended to change the classification of the funds. Thus, the court held that the real estate was the wife's separate property.

The court in *Conley v. Quinn*, 346 P.2d 1030 (N.M.1959), reached a similar result. The husband owned a large farm that was separate property. Under New Mexico law, the income generated by the farm was also separate property. The husband also raised a limited number of cattle, chickens, and hogs, which were community property. When the livestock was sold, the proceeds were deposited into the same account as the income from the crops. This commingling was held to be de minimis and not to change the separate classification of the account. Consistent with this view is *Noble v. Noble*, 546 P.2d 358 (Ariz. Ct. App. 1976). In that case, the husband deposited \$3,000 of his earnings in his wife's bank account and then claimed that all subsequent assets purchased through the account were community property. The court rejected this assertion.

Although the cases do not decide the issue, a spouse should be obligated to reimburse the other spouse for the amount of marital property added to the commingled fund, assuming the appropriate

amount can be determined. This approach is based in equity and prevents nominal commingling by one spouse from producing a windfall to the other spouse.

## 7. Other Rules [§ 3.24]

When the spouses do not keep sufficient records for satisfactory tracing under any of the above rules, the courts must decide whether to follow the presumption that all the spouses' assets are marital property or to use equitable powers to establish a portion of the assets as individual property. This issue normally arises when a new investment is made and no special presumption arises from the nature of the expenditure, such as the purchase of a security. In this situation the court might determine itself bound by the presumption and classify all assets as marital property. However, if, for example, a spouse establishes an inheritance of \$100,000 and is unable to trace the funds, but the aggregate assets of the couple increases, a court can probably consider the equities of the case. For this purpose, it is unclear whether ordinary accounting rules will be helpful. George Gleason Bogert & George Taylor Bogert, *The Law of Trusts and Trustees* §§ 926-28 (3d ed. 2007). See the discussion of Wisconsin's rejection of equitable tracing in divorce at section 3.23, *supra*.

If a court decides it is not bound to follow the presumption that all the assets are marital property, it has several options. It can use the reverse of the maximum-marital-benefit approach of *Duncan* discussed in section 3.22, *supra*, and give the spouse establishing untraceable individual property a pro rata interest in the assets. Alternatively, the court could assume that all the community funds are withdrawn first. *Barrington v. Barrington*, 290 S.W.2d 297 (Tex. Ct. App. 1956). A final approach would be to allocate all the investments to the community but allow the separate estate a reimbursement claim. *Horlock v. Horlock*, 533 S.W.2d 52 (Tex. Ct. App. 1975); *Succession of Videau*, 197 So. 2d 655 (La. Ct. App. 1967). This final approach is similar to the procedure followed in divorce actions in Wisconsin and has been used in Texas and Louisiana, two of the three states that, like Wisconsin, provide that income on separate property is community—or “marital”—property.

The failure to sufficiently identify nonmarital property in a commingled account can have consequences beyond the mere reclassification of the account balance to marital property. In *Swope v.*

*Swope*, 739 P.2d 273 (Idaho 1987), the husband had a bank account before marriage. During the marriage, all the family's income and other cash receipts were deposited into this account, which was later made into a joint account. The husband had paid a premarital obligation from this account. Because of the commingling, the court found that the balance in the account was community property. Thus, the payment of the husband's premarital obligation was found to have been made with community funds, and the wife was entitled to reimbursement for one-half the amount so paid.

The various methods of sorting out commingled assets are doctrines of equity. Thus, evidence that commingled funds have been partly wasted (such as by supporting a gambling, liquor, or drug habit) may bar the use of tracing-based theories to establish individual property. *Anstutz*, 112 Wis. 2d 10; *see also* *Reppy & Samuel*, *supra* § 3.12, at 126–28.

### **C. Tracing Concerns Involving Other Assets [§ 3.25]**

Mixing (i.e., commingling) can occur with regard to assets other than money. Whenever commingling occurs under section 766.63(1), regardless of the type of asset, the courts must determine whether any individual (i.e., separate) property can be identified. The following sections discuss various situations from other community property jurisdictions that have faced this problem. The cases may prove helpful in applying the Act.

#### **1. Accounts Receivable [§ 3.26]**

One of the assets a spouse may bring to the marriage as individual property is a business's accounts receivable. In the typical situation, the spouse's business continues after marriage, the original accounts receivable are collected, and new accounts receivable come into existence. At termination of the marriage, the issue is whether any of the accounts receivable at termination are classified as individual property. Normally, none of the accounts receivable at termination are so classified.

For example, in *House v. House*, 123 Cal. Rptr. 451 (Ct. App. 1975), the husband was a physician who came into the marriage with accounts



receivable from his medical practice. These represented a separate asset. At divorce, he requested that an amount of current accounts receivable equal to what he had brought into the marriage be allocated as his separate property. The court held that the current accounts receivable were all community property because they were earned during the marriage. The receivables brought into the marriage were spent for community purposes and acquisitions, but without an agreement for reimbursement. The court therefore held that the husband had made a contribution to the marriage and the community for which he could not recover.

## **2. Minerals and Wasting Assets [§ 3.27]**

If a spouse owns an interest in a mineral deposit as individual property, a mixing issue arises when the mineral interest is developed. If the coal, oil, or other mineral is considered income, its development reclassifies the entire asset to marital property. *See supra* § 2.39. On the other hand, if the mineral proceeds are considered a return of capital, the marital estate obtains no return from the individual asset even though income on individual property would be marital property. *See supra* § 2.39.

The issue is further complicated if marital funds are used to develop the asset or if a spouse performs substantial labor in connection with the development. The alternatives are to allocate “all or nothing” to the individual interest based on the preponderance of value contributed or to make an equitable apportionment between the two interests. The all-or-nothing rule provides certainty but can produce arbitrary results. The equitable-apportionment approach is difficult because the portions are not known when received; thus, subsequent mixing of funds is unavoidable.

The all-or-nothing approach was used in *Norris v. Vaughan*, 260 S.W.2d 676 (Tex. 1953). The spouses were married for six years. Before the marriage, the husband owned an undivided interest in seven gas-producing wells as a lessee, plus two undivided partnership interests, one a one-quarter interest and one a one-half interest, in two oil and gas partnerships. The wells produced gas during the term of the marriage under contracts, entered into before the marriage, covering the life of production. The husband expended little effort in managing the properties.

The court found that the production of natural gas would eventually exhaust the gas reserves that comprised the separate estate. The court considered this equivalent to a piecemeal sale of the separate corpus and held that the funds acquired through a sale of the separate corpus, if traced, would remain separate property. This is consistent with the treatment of a lessor of the interest to whom royalties are paid when oil or gas is produced, the royalty payments being for extraction or waste of the separate estate and, therefore, classified as separate property. (The estate had acknowledged that the gas was separate property while it was in the ground, but had argued that the profits on the sale of the gas were community income. In Texas, most judicial determinations historically allocate all or nothing to the community.)

The *Norris* court distinguished two earlier cases in which a complete change of classification of an asset had been found to occur as a result of the asset's development. One of those cases involved bricks made from clay that had been extracted from land that was separate property; the other case involved finished lumber that was sold after having been sawed from timber classified as separate property. In both cases, unlike in *Norris*, there had been a great deal of community effort "required to transmute the separate property into a new and more valuable state." *Id.* at 680.

With regard to the partnership interests in *Norris*, the court initially looked to the gas wells the partnership owned at the time of the parties' marriage. The court held that the husband had the sole right to manage, control, and dispose of his separate property during marriage and that this included reasonable control and management necessary to preserve the separate estate and to put it to productive use. Thus, activities relating to the maintenance and production of the minerals would not cause a part of those minerals to be reclassified as community property.

In contrast to the all-or-nothing rule followed in *Norris*, the allocation rule is more equitable and will probably find judicial favor in Wisconsin. If this occurs, it will be beneficial to adopt some clear standards, such as that the individual interest receives the cash flow until complete recovery of the value of the asset before development. In addition, because allocation is impossible at the time of receipt, the claim should be one of reimbursement rather than of ownership. The partnership analysis was changed when Texas enacted the Uniform Partnership Act. *Marshall v. Marshall*, 735 S.W.2d 587 (Tex. Ct. App. 1987).

### 3. Securities and Securities Accounts [§ 3.28]

Individual securities may become mixed property through trading if proceeds from the sale of securities are deposited into a commingled account and subsequent purchases are made from that account. Mixing may also occur when individual securities are placed in an account having marital property securities if both classifications of securities are later sold and the proceeds reinvested. A third mixing situation may occur if a security in a dividend reinvestment plan is sold and the proceeds are reinvested without allocating the proceeds between individual and marital property. This problem also occurs if the securities account is a margin account, amounts are borrowed to purchase securities, and repayment of the margin debt is made from sources having a different classification.

These situations were considered in *Marsden v. Marsden*, 181 Cal. Rptr. 910 (Ct. App. 1982). The husband contended that a number of securities maintained in a single securities account were his separate property. Before marriage, the husband owned a substantial amount of securities and had a savings account. During the marriage, the husband had a checking account into which his wages were automatically deposited. While the parties were married, the husband engaged in numerous transactions involving the sale and purchase of securities. The proceeds from some sales were deposited in the account into which his salary was deposited, and the husband acknowledged that it was impossible to identify the separate funds in this account. Some securities purchases also were paid for from this same account.

The certified public accountant hired to log the stock transactions admitted that if a stock had been purchased from funds in the checking account and then later sold and the proceeds deposited in the savings account, his worksheet would not show that the funds were originally from the commingled account. The accountant's figures identified the aggregate amounts purchased and sold for each year, and the accountant concluded that sufficient separate funds existed to purchase the securities. (This approach is similar to recapitulation of community income and expense.)

The court stated that the husband could have avoided this difficulty by contemporaneous, rudimentary record keeping. The court applied the presumption that a purchase of property during the marriage with funds from an undisclosed or disputed source, such as an account or fund in

which property has been commingled, is community property. The burden of establishing a spouse's separate interest in presumptive community property involves more than simply presenting proof at the time of litigation; it also requires keeping adequate records throughout the period of marriage. The court held that the professional reconstruction of records by the accountant was inadequate and awarded the husband only those securities that he never traded during the marriage.

The securities account was a margin account, and at the time of trial there was a margin-account debt of \$38,000. The court did not permit deduction of this amount from the securities determined by the court to be community property because the husband did not introduce any evidence that the margin-account debt related to any of the securities determined to be community property.

In Wisconsin, margin-account debt should be classified when the debt is incurred. If a debt is incurred during the marriage, it is usually for a family purpose, and the assets thereby acquired are marital property. However, when the debt involves a margin account, it is arguable that the lender is looking primarily to the collateral (securities) in the account for repayment rather than to the income stream of the spouse. The classification of the debt determines the initial classification of the asset acquired. If the debt is subsequently satisfied from funds of a different classification, the issue of reimbursement versus ownership arises. *See infra* § 3.39.

#### **4. Casualty Insurance [§ 3.29]**

A building or tangible personal property asset identified as a spouse's individual property is normally insured against a casualty loss. If the premium on the casualty insurance is paid from marital property and a loss subsequently occurs, do the insurance proceeds take the classification of the asset insured or the classification of the insurance policy?

The court considered the situation in *Trahan v. Trahan*, 387 So. 2d 35 (La. Ct. App. 1980). Before marriage, the husband acquired as his separate property what later became the marital residence. The homeowner's insurance policy on the property was in the husband's name, but during the marriage he paid the \$300 premium using

community funds. A fire occurred, and the insurance company paid the husband \$46,560.

The question was whether the premium payment from the community funds caused the insurance proceeds to be classified as community property. The court held that it was the classification of the property insured, not the source of the premium payment, that determined the classification of the proceeds. Consequently, the community only had a right to reimbursement for the amount of the premiums paid. *See Saslow v. Saslow*, 710 P.2d 346 (Cal. 1985) (achieving same result regarding use of community property funds to pay premiums on private disability insurance contract and for payment of premiums for waiver of premium benefit in the event of disability on life insurance policies); *see also In re Marriage of Pearson-Maines*, 855 P.2d 1210 (Wash. Ct. App. 1993).

This result seems appropriate under Wisconsin's Act also, because although section 766.63(1) is predisposed toward the creation of ownership interests in situations in which marital property is expended, classifying the proceeds based on the source of the premium payment rather than on the classification of the property insured would convert a casualty loss on separate property to an inequitable windfall to the community. *See Bille v. Zuraff (In re Estate of Bille)*, 198 Wis. 2d 867, 543 N.W.2d 568 (1995) (regarding life insurance to secure a mortgage).

## **5. Income Tax Savings [§ 3.30]**

During marriage, spouses frequently file joint income tax returns to reduce their tax liability. Is the amount of tax savings obtained through filing a joint income tax return, as compared to the tax obligation from filing separately, a marital asset? (This issue is different from the classification of an income tax refund.)

*Bowart v. Bowart*, 625 P.2d 920 (Ariz. Ct. App. 1980), concerned a husband's attempt to have the tax benefits realized from filing a joint return during marriage treated like community property, with the tax benefits analogous to retirement benefits and profit-sharing funds. Almost all the income reported on the returns was the wife's separate property. The court stated that the tax benefits from a joint return should not be treated like retirement benefits and should not be deemed community property. If community funds are used to pay a separate

income tax obligation, a right of reimbursement is created. *Saslow*, 710 P.2d 346.

## **D. Acquisition of Property [§ 3.31]**

### **1. Single Payment in Full [§ 3.32]**

After the initial classification of funds, the spouses' rights in assets purchased with those funds must be evaluated. If the property is acquired with a lump-sum payment that is partly marital property and partly individual property, a form of co-ownership results that recognizes the marital and individual ownership of each component. This is the rule in Wisconsin—*see* Wis. Stat. § 766.63(1)—and in all the community property states except Louisiana. *Reppy & Samuel, supra* § 3.12, at 80.

### **2. Acquisition on Credit—Classification of Debt [§ 3.33]**

Most major acquisitions involve a loan. The loan may be a purchase money loan or a loan separate from the property acquired; in the latter case, the loan may be secured or unsecured. A loan raises two primary issues: first, its effect on the initial classification of the asset; and, second, whether the classification changes over time, based on the source of the payments used to reduce the debt. *See* William Q. de Funiak & Michael J. Vaughn, *Principles of Community Property* § 78 (1971 ed.).

In classifying an asset, all community property states consider the debt, and although they use different methods of analysis, all community property states presume that loans incurred during marriage are community obligations and that the loan proceeds and assets acquired with those proceeds are thus community property. An asset's classification is not determined solely by analysis of the funds used for the down payment. When an asset is purchased on credit before marriage, the entire asset is the acquiring spouse's individual property. The issue of what happens when an individual debt is satisfied with marital property is addressed in a later section.

Where property has been purchased with borrowed funds, the courts in classifying the property look to the point in time when consideration is

paid and title passes. When the seller parts with title upon being given a promissory note by a spouse, the effect is as if borrowed money had been used to make the acquisition, even though funds do not actually change hands. The historic rule is that the source of the funds used to discharge the loan, whether separate or community funds, does not affect the classification of the items purchased with the proceeds. The source does, however, give rise to a question of right of reimbursement. *Freeburn v. Freeburn*, 620 P.2d 773 (Idaho 1980).

If items purchased with borrowed funds are on hand at dissolution of the marriage or death, the items must be classified. While all the other community property states presume that loans during marriage are community obligations, the strength of the presumption and the method of analysis differ among the states. Texas has the easiest rule to apply for classifying credit acquisitions. It provides that all credit acquisitions during marriage are community property unless there is “clear and satisfactory evidence that the creditor agreed to look solely to the separate estate of the contracting spouse for satisfaction.” *Mortenson v. Trammell*, 604 S.W.2d 269, 275 (Tex. Ct. App. 1980) (writ. ref’d n.r.e.). But see *Carter v. Carter*, 736 S.W.2d 775 (Tex. Ct. App. 1987), in which a margin debt was used to acquire securities and was subsequently satisfied from the proceeds from selling securities in the account. The court did not consider the margin debt to have caused any of the securities in the account to become community property. Similarly, in Nevada, proceeds of unsecured loans given on personal credit of the husband or wife are presumed to be community property. *Jones v. Edwards*, 245 P. 292 (Nev. 1926).

In California and Idaho, and apparently in Arizona and Washington, the presumption that the asset is community property is rebutted by showing that the lender made the loan based on a belief that the existence of separate property of the borrower made repayment likely. See *Shovlain v. Shovlain*, 305 P.2d 737 (Idaho 1956); *Finley v. Finley*, 287 P.2d 475 (Wash. 1955).

On the other hand, if a borrower in California, Idaho, Arizona, or Washington pledges separate property as security, the proceeds are presumed separate. See *Freeburn v. Freeburn*, 555 P.2d 385 (Idaho 1976). But what happens if the separate property pledged as security is the same property purchased with the loan proceeds after a down payment of separate property? Does a five percent down payment made with separate funds render the entire acquisition separate? Does the

other spouse's signature on the contract of purchase or mortgage note make the asset community property? When an asset is acquired during marriage and a debt is incurred, the other community property states use three approaches to determine the initial classification of the asset. One approach was set forth in *Cargill v. Hancock*, 444 P.2d 421 (Idaho 1968). The court held that the property was separate on the theory that simply incurring debt or signing the purchase contract was not enough to create community property; it was also necessary to make subsequent payments from community funds. Using a second approach, other community property states have found the signature alone sufficient to make the proceeds community property. *Finley*, 287 P.2d 475; *see also* Reppy & Samuel, *supra* § 3.12, at 93–96.

A third approach to determining the classification of an asset using funds obtained through a loan is found in California, where if money for the purchase of property is obtained on the credit of the community estate, the result is a community purchase. The lender's intent regarding the credit at the time the credit is given determines whether the community estate's credit has been used. In this respect, photographs and statements made after the purchase are not relevant.

*Ford v. Ford*, 80 Cal. Rptr. 435 (Ct. App. 1969), illustrates this approach. The spouses at all times were residents of California. The husband purchased a farm in Illinois by obtaining a bank loan. The note was signed by the spouses and was secured by a mortgage on two Illinois farms, also signed by both spouses. Payments on the note were made from the farm income, and there was no substantial evidence that the husband contributed his time, energy, or talent to the operation of the farms. The issue at divorce was whether the purchased farm was community property, based on the debt used for its purchase. Since there was no evidence that the bank considered the wife's occupation or income in granting the loan, the central issue was whether the wife's signatures on the note and mortgage indicated, in and of themselves, an intention on the part of the bank to hold the community estate responsible for payment.

Although the wife's signature on the note and mortgage raised the inference that if she had not executed the documents, credit would not have been extended, earlier California cases had held that a signature alone could not affect the rights of the parties. Consequently, the court in *Ford* held that the loan was a separate loan and the farm was the husband's separate property.



In Wisconsin, when an asset is acquired on credit during the marriage, the debt must be analyzed. If the debt were not considered, the down payment would be given undue weight, i.e., all appreciation or depreciation would follow the classification of the down payment. In Wisconsin, it appears that the first step in analyzing the debt is to determine the nature of the obligation created. That is, was the obligation incurred in the interest of the marriage or the family? If the obligation was incurred in the interest of the marriage or the family, the debt usually may be satisfied from all marital property. Wis. Stat. § 766.55(2)(b).

This approach follows the family-purpose doctrine used in Arizona, Louisiana, and Washington. In Wisconsin, almost all investment transactions are in the interest of the marriage or the family and thus may obligate all the marital property, whether or not the note is signed by both spouses. Given the obligation of marital property to satisfy the debt, it is likely that Wisconsin will develop a strong presumption that loan proceeds are marital property and that the asset they purchase is marital property.

The second step in analyzing the debt is to look at the specific circumstances of the loan. Not all loans incurred in the interest of the marriage or the family will be satisfied from marital property. For instance, in a situation in which a creditor has agreed to look only to individual property and predetermination date property, the debt will not necessarily be satisfied from marital property. See Wis. Stat. § 766.55(4).

Another instance in which the marital property result might not occur is one in which all the security for a loan is the individual property of the contracting spouse, and the individual security is not the asset being acquired. An additional instance is one in which there is no personal liability on the loan, and the creditor is looking only to the collateral, such as a loan against a life insurance policy. In that instance, the classification of the collateral should determine the classification of the loan proceeds.

### **3. Acquisition over Time [§ 3.34]**

In addition to acquisitions made with a single payment, acquisitions during marriage may be made in which the consideration is paid over

time. In situations in which payment is in installments, title may be received immediately or after all payments are made. A land contract is the most frequently occurring type of transaction in which transfer of title is deferred.

When payment is over time, the issue is whether the property classification should be made at acquisition, when title is received, or periodically as the payments are made. It is also possible to find a gift between the spouses affecting classification, although in the acquisition situation, in contrast to some other situations, a gift is not presumed.

The community property states have developed three ways of determining ownership when payment is made over time. These three ways, the pro rata approach, the inception-of-title approach, and the time-of-receipt approach, are described below. The time-of-inception approach is most widely used in the other community property states but, as discussed below, Wisconsin is expected to use the pro rata approach.

No state uses a single theory consistently for all kinds of acquisitions occurring over time. Louisiana uses a time-of-vesting theory for real estate acquisitions, including those by adverse possession, but uses an acquisition-of-title theory for acquisitions of personal property and a pro rata theory for pensions. In California, an inception-of-right theory is used for adverse possession cases, a pro rata theory for installment purchase contracts, and a time-of-vesting theory in some deferred compensation contract cases. Reppy & Samuel, *supra* § 3.12, at 82. The classification question normally arises in the other community property states when title is in one spouse's name.

#### **a. Pro Rata Approach [§ 3.35]**

The pro rata (or tracing) approach provides for concurrent ownership like the concurrent ownership that stems from a lump-sum purchase. Reppy & Samuel, *supra* § 3.12, at 81. The focus is on the overall percent of consideration paid over time from each classification of property.

In existing community property jurisdictions, the pro rata approach has most frequently been followed in cases involving insurance and retirement benefits. *See, e.g., Sims v. Sims*, 358 So. 2d 919 (La. 1978); *Porter v. MacLeod*, 553 P.2d 117 (Wash. Ct. App. 1976). It has also

been used in some cases involving installment-purchase contracts. *See, e.g., Giacomazzi v. Rowe*, 240 P.2d 1020 (Cal. Ct. App. 1952); *Maskuns v. Maskuns*, 268 P. 1093 (Cal. Ct. App. 1928). On the other hand, the approach has been considered and rejected in some jurisdictions. *See, e.g., In re Marriage of Harshman*, 567 P.2d 667 (Wash. Ct. App. 1977); *McCurdy v. McCurdy*, 372 S.W.2d 381 (Tex. Ct. App. 1963) (writ ref'd). One problem with the pro rata approach involves determining the appropriate pro rata shares. The California cases have treated the initial payments made years before the debt was fully satisfied as buying the same share of ownership as the last payment. If the obligation is amortized over time, as occurs in the typical mortgage situation, the payment amount remains constant, but the initial monthly payments are nearly all interest and the later payments nearly all principal, and only the principal portion is considered in determining the pro rata ownership of each classification. Reppy & Samuel, *supra* § 3.12, at 82–83.

In Wisconsin, it is likely that preference will be given to the pro rata or tracing approach because the ownership interests created are most consistent with the source of payment. The pro rata approach best recognizes the statutory intent that an ownership interest be created when property is mixed, and the approach permits each interest to share in the appreciation or depreciation of an investment in proportion to its respective contribution. *See* Wis. Stat. § 766.63.

### **b. Inception-of-title Approach [§ 3.36]**

The inception-of-title approach focuses on the initiation of the transaction. Under this rule, if one spouse enters into a purchase contract before marriage, the property is separate even though all payments are made during marriage from community property. The community has a claim only for reimbursement. On the other hand, if one spouse enters into a purchase contract during the marriage, the property may be community property even though all payments are made from separate property. The spouse's separate estate has a claim only for reimbursement.

The inception-of-title approach is illustrated in *Winn v. Winn*, 673 P.2d 411 (Idaho 1983), which involved an installment purchase by a husband and wife of their principal residence. The spouses purchased a house, and the husband paid the earnest money and the down payment from his separate funds. A loan for the remaining purchase amount was

secured by a deed of trust on the house. Although both spouses were named in the contract and signed the promissory note and deed of trust, all payments during the marriage were made from the husband's separate funds. When the parties filed for divorce, the question was whether the residence was community property even though all payments had been made from separate property.

Under the inception-of-title approach, it is crucial to ascertain when property purchased through credit is acquired for the purposes of community property law; the answer "lies in the basic rule that 'the character of an item of property as community or separate vests at the time of acquisition.'" *Id.* at 414; *see also Freeburn v. Freeburn*, 555 P.2d 385 (Idaho 1976). Property purchased with money borrowed by either spouse during the existence of the community is presumed community property. Moreover, the property cannot be gradually converted from community property to separate property by one spouse making payments on a community debt from his or her separate funds. Otherwise, one spouse could unilaterally transform the property's classification, violating the doctrine that the classification of property may be changed only by agreement between the spouses.

Most commonly, the collateral for the loan is the very asset for which the loan is obtained. When, however, security is provided for a loan apart from the asset being acquired, the rule is different. The loan proceeds made upon the security of one spouse's separate estate are sometimes separate, whereas those made upon the security of the community estate are community. Finally, under the inception-of-title approach, an agreement as to the classification of an asset controls.

The court in *Winn* held that the loan was a community loan, and thus, the character of the entire property was community. The holding was based on the fact that the house was deeded to both the husband and wife and that each had signed the promissory note and deed of trust. Furthermore, the lender's first option in the case of default would have been to foreclose on the property. In reaching its conclusion, the court considered the liability of the community for the loan, the source of repayment, the basis of credit upon which the lender relied, the source of the down payment, the names on the deed, and which parties signed the loan documents.

The court did not allocate a proportionate interest in the home to the husband's separate estate based on his down payment. The court did

give the husband a right to reimbursement for the payments from his separate funds made on the community obligation in the absence of a finding that the contributions were intended as a gift to the community. The court also found that after the wife left the residence, she was entitled to receive one-half of the fair rental value of the property as rental for the husband's occupancy. For other illustrations of the inception of title approach, see *McCurdy*, 372 S.W.2d 381; *Carter v. Carter*, 736 S.W.2d 775 (Tex. Ct. App. 1987); and *Potthoff v. Potthoff*, 627 P.2d 708 (Ariz. Ct. App. 1981). See also *McVay v. Parrish (In re Parrish)*, 161 B.R. 785 (W.D. Tex. 1992), *aff'd*, 7 F.3d 76 (5th Cir. 1993).

The inception-of-title approach will probably not be the general rule used in Wisconsin. Both the Act's definition of acquiring and the comments to UMPA indicate that satisfaction of a debt creates an ownership interest. The Act appears to reject the concern of change of classification from the unilateral action of one spouse.

### **c. Time-of-receipt Approach [§ 3.37]**

The time-of-receipt approach is used when receipt of title is deferred. This approach focuses on the marital status when the unencumbered title is received or the transaction is closed. The source of payments for the purchase is not determinative unless the entire consideration was paid from separate funds. If a community contribution was made, the separate estate has only a right of reimbursement. *Reppy & Samuel, supra* § 3.12, at 81. This approach has not been widely accepted outside Louisiana. It may, however, be equitable in adverse possession situations, when no interest arises until the entire period has expired.

This approach was explained in *Cosey v. Cosey*, 364 So. 2d 186 (La. Ct. App. 1978), *aff'd*, 376 So. 2d 486 (La. 1979). In *Cosey*, the husband entered into a bond-for-deed contract to purchase real estate during his first marriage. The contract was paid during that marriage using community funds. After the last payment, but before title was delivered, the couple divorced and the husband remarried. Thereafter the owners of the real property acquired good title and issued a deed to the husband and his second wife. The first wife died, and twelve years later the husband died survived by his second wife. The administrator of the husband's estate brought an action against the second wife, asking that the parcel of real estate be found to be community property of the first marriage.

The intermediate court held that because the title was acquired during the second marriage, the property belonged to the community of the husband and his second wife. The supreme court reversed on the ground that under the facts of the case, title vested when the vendor was contractually obligated to have delivered the deed. Because that point was when the final payment was made, the real estate was community property of the first marriage.

### **E. Transmutation to Joint Tenancy or Tenancy in Common [§ 3.38]**

The other community property states find that title taken by the spouses in joint tenancy or tenancy in common are ownership forms inconsistent with community property. Thus, if community property funds are used to acquire an asset in joint tenancy or tenancy in common, the community is not entitled to reimbursement. The parties have the ownership rights of joint tenants or tenants in common. Community property ownership and reimbursement theories do not apply unless otherwise expressly provided by statute. *Gonzales v. Gonzales*, 172 Cal. Rptr. 179 (Ct. App. 1981); Cal. Fam. Code Ann. §§ 2581, 2640 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 20 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot).

In Wisconsin, after the determination date, spouses can only create a joint tenancy or tenancy in common exclusively between themselves by using a marital agreement. Other attempts are ineffective. An attempt to create a joint tenancy will create survivorship marital property; an attempt to create a tenancy in common will create marital property. Wis. Stat. § 766.60(4)(b). Thus, an unintentional reclassification of individual property or predetermination-date property may occur if one spouse attempts to place the individual or predetermination-date property in a joint tenancy or tenancy in common with the other spouse.

A joint tenancy or tenancy in common between spouses can be created by spouses after the determination date only under a marital agreement. The terms of the marital agreement will govern the disposition and respective rights in the joint tenancy. If the agreement has no provisions governing the disposition and rights, the rules applied in the other community property states should apply. Thus, if under a marital agreement and after the determination date, spouses place marital

property in a joint tenancy between themselves, that should constitute a transformation in the character of the asset. The result is that joint-tenancy rules rather than marital property rules apply to the asset. *See supra* § 2.252. If the joint tenancy so created is terminated, it is unclear whether the funds received are transformed back to marital property, or whether they become individual property of the spouses.

The conclusion that a transformation has occurred is consistent with the analysis in a number of Wisconsin divorce decisions. In *Trattles v. Trattles*, 126 Wis. 2d 219, 376 N.W.2d 379 (Ct. App. 1985), the wife deposited gifts from her father either in a separate bank account in her name or in a joint bank account. The funds were used for household furnishings, normal household expenditures, maintenance and improvements, and various mortgage payments on the residence owned in joint tenancy between the spouses. There was no express evidence of the wife's intention to make a gift to her husband of the funds received from her father. The court held, however, that the actions of the wife in using the gift proceeds on the jointly owned home and for the benefit of the family served as evidence of her donative intent.

The court concluded that the character of all property received by gift was altered so as to render its present form property subject to division under section 767.255 (now numbered section 767.61). The transfer of inherited property to joint tenancy changes the character of the ownership in the entire property to property subject to division. With regard to expenditures for household furnishings not titled in the name of either spouse, the court examined the way the parties treated the property to determine if its character had been altered. The court found that because the items in this case were usually purchased for the mutual enjoyment and use of both spouses, it was appropriate to infer such transmutation. *See also Bonnell*, 117 Wis. 2d 241; *Weiss*, 122 Wis. 2d 688.

In *Fowler*, 158 Wis. 2d 508, the wife received cash gifts from her father, a portion of which were deposited in a joint checking account. Funds from the joint checking account were later used to purchase securities registered in her sole name. The issue was whether, for property division in a divorce, the securities were property acquired by gift or inheritance. The court held that by depositing the funds in a joint checking account, the wife intended to make a gift to the family. The deposit caused the property to lose its character as property acquired by gift or inheritance. This is the first case holding that a deposit into a joint

bank account, being a statutory creation as opposed to a true common law joint tenancy, is sufficient to change the character of the funds deposited.

The parties in *Steinmann v. Steinmann*, 2008 WI 43, 309 Wis. 2d 29, 749 N.W.2d 145, were married in 1994 and began divorce proceedings in 2004. Both parties had been previously married. During the marriage, the parties entered into a limited marital property classification agreement, which provided that all property listed on Schedule A was the respective individual property of each party, all earnings of each party after the date of marriage were the individual property of the earning party, and all property acquired from a third party by gift or inheritance was the individual property of the recipient spouse. The classification of assets was to determine property division in the event of a divorce. The agreement was backdated to March 3, 1995. In a separate proceeding, the court determined that the agreement was valid and binding on the court for property division purposes.

During the marriage, the wife used her individual property as classified by the agreement to purchase three residential properties and two boat slips, all of which were jointly titled. The issue before the court was whether the rules of tracing and transmutation (character and identity) were applicable to determining whether the jointly titled assets owned at the time of divorce were divisible. The identity and character doctrines assist courts in determining whether an asset was acquired by gift or inheritance and, if so, is specifically exempted by statute from property division. The wife advocated that tracing be applied and argued that if tracing was utilized, it would establish that all the jointly titled properties were in fact her individual property. The husband argued that the court should not use tracing but instead should apply the transmutation rules, and that this would result in the jointly titled property being divisible in divorce. The supreme court held that the character and identity analysis that is applied for determination of gifted and inherited property could properly be used to determine which assets were divisible when applying a marital property agreement. Pursuant to those rules, the parties' use of nondivisible property to purchase assets that were then titled jointly caused the assets to become divisible property.

The Act includes a statutory terminable marital property classification agreement and a statutory terminable individual property classification agreement. Wis. Stat. §§ 766.588, .589; *see also infra* §§ 7.73, .83.



Although the statutory agreements as originally enacted dealt with the property law consequences of the agreements upon assets owned in joint tenancy or tenancy in common, it was unclear whether those agreements affected funds held in a joint account created under chapter 705. Both agreements provided that to the extent the incidents of joint tenancy conflicted with or differed from the incidents of individual property or marital property, respectively, the incidents of joint tenancy, including the incident of survivorship, control. Wis. Stat. §§ 766.588(1)(c)4., .589(1)(c)2. The uncertainty arose because joint accounts are not traditional joint tenancies. Assets classified as individual property or as marital property would not have the survivorship feature. The Act was amended by the 1992 Trailer Bill to clarify that the statutory agreements under sections 766.588 and 766.589 do not affect the incidents of joint accounts under chapter 705, including the incident of survivorship. Wis. Stat. §§ 766.588(1)(d)2., .589(1)(c)1.

In addition to being used to create a new joint tenancy after the determination date, marital property may be added to a joint tenancy or tenancy in common created before the determination date. The classification of marital property added to a joint tenancy or tenancy in common is discussed at sections 2.252–.260, *supra*.

Under the Act, when marital property is added to a joint tenancy or tenancy in common, if the incidents of the joint tenancy or tenancy in common conflict with or differ from the incidents of the property classification under chapter 766, then the incidents of the joint tenancy or tenancy in common, including the joint tenancy incident of survivorship, control. Wis. Stat. § 766.60(4)(a). The marital property added to the preexisting joint tenancy or tenancy in common is not, however, reclassified. Instead, the addition of marital property to a preexisting joint tenancy invokes application of the general mixing rules of section 766.63(1).

## **F. Satisfying Debts or Making Improvements with Property of a Different Classification [§ 3.39]**

An asset's initial classification is determined when it is acquired. A question arises when funds of a different classification are thereafter used to reduce indebtedness or improve the property. This is different from the situation in section 3.34, *supra*, because in this situation a classification of the asset has occurred, normally because of inheritance,

gift, or acquisition before marriage, and community property is subsequently used to reduce the debt. For example, if a spouse inherits a cottage and finances a substantial addition to it with marital property, does the cottage remain entirely individual property? As a further example, if a residence acquired before marriage has a mortgage and payments on the mortgage are made in part with marital property, does the residence remain entirely individual property? The steps to analyze this issue are discussed in the following sections.

### **1. Gift Analysis [§ 3.40]**

When considering the effect of subsequent payments using funds of a different classification, the first inquiry is whether a gift has been made. *See Washington Deskbook, supra* § 3.20 (discussion of gift rules). If a gift is established, the mixing rules of section 766.63 do not apply. No gift is presumed if marital property is used by a spouse to improve his or her individual or predetermination date property. *See Warren v. Warren*, 104 Cal. Rptr. 860 (Ct. App. 1972). If, however, one spouse uses marital property to improve the other spouse's individual property or predetermination date property or uses his or her individual property or predetermination date property to improve marital property, a gift may be found. California, Idaho, Arizona, and Nevada generally presume a gift was made in these situations. *Cooper v. Cooper*, 635 P.2d 850 (Ariz. 1981); *Warren*, 104 Cal. Rptr. 860; *Shovlain v. Shovlain*, 305 P.2d 737 (Idaho 1956); *Lombardi v. Lombardi*, 195 P. 93 (Nev. 1921). (Many of these cases were decided before the change to a community property system based on equal management and control; this change should not affect the result, however.) It is possible to rebut the gift presumption, and rebuttal testimony by spouses has generally been accepted.

In Wisconsin, the Act does not indicate whether a gift is presumed. In early drafts of the Act, gift presumptions were included. These were not incorporated in the Act as adopted, and it appears likely that Wisconsin will use the mixing statute and not utilize gift presumptions. However, in each instance in which an improvement is made or indebtedness is reduced using property of a different classification, it is necessary to determine whether a gift was in fact made before applying the mixing statute. Finally, in Wisconsin, the limit on the amount of gifts does not apply because the gift is to a spouse and not a third party. Wis. Stat. § 766.53.

The gift analysis was applied in *Warren*, 104 Cal. Rptr. 860. In California, when a spouse uses community funds to improve his or her own real property, a form of the tracing doctrine applies to prevent the spouse from profiting from a constructive breach of fiduciary duty to the other spouse. When, however, one spouse uses community funds to improve the separate property of the other spouse, there is no tracing, and any right to reimbursement is made solely on the basis of a specific agreement.

In *Warren*, the spouses stipulated that \$38,000 of community funds were used during marriage to improve a building that was initially the wife's separate property. At the time of divorce, the building was worth only \$33,952. The court found that no gift was intended. The court stated that reimbursement was based on the commingling that constituted a breach of trust; the injured party (the husband) was entitled to the amount expended or the enhanced value, whichever was greater. Thus, the court held that \$38,000 should be reimbursed to the community.

## **2. Satisfaction of Debt [§ 3.41]**

When community funds are used to reduce indebtedness on a separate property purchase-money mortgage or land contract, and no gift was made, most states treat the situation as raising only a right of reimbursement. This is technically correct because title to property purchased with borrowed funds vests at the time of the acquisition of the property, not as repayment of the loan occurs. Subsequent repayment of the loan does not acquire any interest but merely reduces indebtedness. *See Rogers v. Rogers*, 754 S.W.2d 236 (Tex. Ct. App. 1988); *Penick v. Penick*, 783 S.W.2d 194 (Tex. 1988); de Funiak & Vaughn, *supra* § 3.33, at § 78. Nevertheless, some of the other community property states have recognized that reimbursement frequently fails to fairly compensate the community for the benefit realized by the use of the separate property. Thus, these states have permitted the community to acquire an interest in the property as the debt is reduced.

In Wisconsin, whether such payments give rise to a right of reimbursement or create an ownership interest is not stated in the Act or the legislative history. As indicated previously, however, the Act and UMPA have a preference for ownership interests rather than reimbursement rights. *See* Wis. Stat. §§ 766.01(1), .63; UMPA § 14 cmt.; *supra* § 3.12. The Act and UMPA define reducing a debt as a form

of acquiring property. Further, the classification statute does not provide that individual property can be increased through the use of marital property. Wis. Stat. § 766.31. Thus, if no gift is found, it is likely that Wisconsin will use an approach that provides an ownership interest. Some of the other community property states are moving in this direction from the traditional reimbursement rule, and some of the cases that illustrate this move are set out below.

In *Popp v. Popp*, 146 Wis. 2d 778, 432 N.W.2d 600 (Ct. App. 1988), the husband had inherited stock in a closely held corporation. During the marriage, the spouses became contingently liable for nearly \$2 million of corporate debt. The debt was secured by all the business assets, a pledge of the husband's interest in the closely held business itself, and a second mortgage on the parties' homestead. Some of the debt was satisfied from proceeds of the subsequent sale of the parties' homestead. In addition, the corporation purchased tangible personal property (e.g., automobiles, a boat, and camera equipment), which the parties used for their personal benefit. The circuit court held that the parties' personal use of certain corporate assets as well as their pledge of certain marital property assets as collateral for corporate debts caused a change in the character of the stock itself for property division purposes.

The appellate court reversed. It held that using corporate monies for the purchase of tangible items and allowing the items to be used by the spouses personally may have served to transmute those items into divisible property. However, this use was not sufficient to transmute the corporate stock into divisible property. The purchase and use of assets was at most a withdrawal from the corporation, like a dividend, and not a commingling of the stock ownership interest.

A character analysis addresses the manner in which the parties have titled or treated the exempt asset. Thus, the inquiry should focus on the asset (here, the stock), not on other assets that may be pledged as collateral against the corporation's debts. In *Popp*, the wife's agreement to accept contingent liability on the company's debts did not affect the character of the exempt assets. *Popp* is a divorce case, but the analysis would be the same in property classification.

*Popp* supports the conclusion that marital property assets and income can be used to secure a loan to a corporation, the stock of which is classified as individual property, without changing the classification of

the stock. This would not be the case if a capital contribution were made or if the business were conducted as a sole proprietorship.

In *Derr v. Derr*, 2005 WI App 63, 280 Wis. 2d 681, 696 N.W.2d 170, the husband's parents gave him a 27-unit apartment building, titled in his sole name, during his marriage. Five years later, both spouses borrowed \$300,000 and used those funds for the benefit of the marriage. Although the couple did not use any of the funds for the apartment building, the \$300,000 loan was secured using the apartment building as collateral. The mortgage note was signed by both spouses, and the mortgage payments were made with marital property funds. At the time of the divorce, \$282,935 remained due on the mortgage loan, and the apartment building had a fair market value of \$905,000. During the marriage, the husband managed the 27-unit apartment building, as well as other smaller apartment buildings. The rental income from these properties was the major source of income for the family.

The court held that the apartment building remained the husband's nondivisible property. However, the court determined that the mortgage debt was divisible and thus should be allocated one-half to each party. The court found that the \$300,000 debt was replaced by \$300,000 of funds that were used for the benefit of the family. The use of marital property funds to reduce that debt only reduced a joint debt of the parties for which they had received cash used in the marriage. The use of the apartment building as collateral did not create a presumption of a gift by the husband to the marriage.

The court agreed that if the marriage purchased an equity in real estate, then that the equity would be divisible. In this case, however, the mortgage payments did not purchase an equity in the apartment building. The payments did not increase the husband's wealth; they reduced a marital debt. The only benefit the husband obtained from the mortgage payments was a reduction in the risk that he created when he used the building as collateral. Thus, the mere act of putting property at risk by using it as collateral for a marital loan does not create a presumption that the owning spouse intended to donate part or all of the property to the marriage.

The Wisconsin approach regarding debt satisfaction may follow the decision in *Torgerson v. Torgerson*, 128 Wis. 2d 465, 383 N.W.2d 506 (Ct. App. 1986). In this case, the wife purchased a duplex solely in her name during the marriage. She used inherited funds for the down

payment. The parties lived in one-half of the duplex and leased the other unit. The mortgage note was signed by the wife alone, but the mortgage itself was signed by both spouses. The mortgage payments were made primarily from the rental proceeds. The husband did not claim that as a result of the manner in which the parties had chosen to treat the property there had been a change in the character of the property attributable to the down payment, but he did contend that the rest of the duplex was purchased with income during the marriage and thus was divisible.

The circuit court held that the duplex was not a divisible asset. The appellate court reversed and held that only the down payment had been made with inherited funds. Property purchased with earnings during the marriage is not excluded from division. The court did not deal with whether any appreciation in the value of the property during the marriage could be allocated to the equity created by the down payment.

*Bille v. Zuraff (In re Estate of Bille)*, 198 Wis. 2d 867, 543 N.W.2d 568 (1995), dealt with a home purchased by the wife before marriage and used as the parties' principal residence during the marriage. At the date of marriage there was an outstanding mortgage on the property and mortgage payments were made from marital property income. In 1986, the balance was paid when a new \$40,000 mortgage was obtained. In 1987, a second mortgage was used for a loan of \$8,688. In 1988, a new loan for \$48,000 was obtained and used to pay off the balance on the two prior loans. All mortgage payments were made from marital property funds. The wife died and the husband claimed the residence was reclassified as marital property.

The court held that the fact that the residence was traceable precluded reclassification. The husband did not present evidence of the total monthly mortgage payments. The court held that (1) when the 1986 loan proceeds were used to satisfy the premarriage obligation, the husband had a remedy to recover one-half of that amount as his individual property; (2) there is a one year statute of limitation on the remedy, and no timely claim was made; and (3) the definition of *acquisition* in the Act does not usurp a valid section 766.63(1) nonmarital-component retention analysis.

In *Noble v. Noble*, 2005 WI App 227, ¶ 20, 287 Wis. 2d 699, 706 N.W.2d 166, the court characterized a number of cases cited by the wife as inapplicable to the issue at hand, namely, whether it constitutes marital waste for a party to fail to secure additional assets that would

have increased the marital estate's value for purposes of property division. Among the cases the court held inconsequential was *Antone v. Antone*, 645 N.W.2d 96 (Minn. 2002), in which the Minnesota Supreme Court set forth another approach for dealing with the appreciation of property acquired before marriage when a mortgage obligation is satisfied during the marriage using marital property funds. In *Antone*, the Minnesota court characterized the equity created through payments made with marital funds to reduce a mortgage on a property acquired before marriage as divisible property. The *Antone* court allocated the appreciation between the divisible and nondivisible property using a formula in which the value of the nonmarital interest at the time of the marriage is compared to the value of the property at the time of marriage and the fraction is multiplied by the value of the property at the time of separation. That portion of the appreciation is not divisible, while the balance is divisible. In *Noble*, the court gave no indication that it would endorse this formula for use in Wisconsin.

The Arizona court allowed a participation in the enhanced value of the asset in *Honnas v. Honnas*, 648 P.2d 1045 (Ariz. 1982). The dispute in that case involved the family residence, which the husband had owned before marriage, and which had substantially appreciated in value during the term of the marriage. During the marriage, two rooms were added that were partially paid for with community funds, a portion of the principal of the mortgage was paid with community funds, and the wife contributed substantial labor and maintenance services to the house.

The court stated that it had discarded the all-or-nothing rule in situations in which appreciation of property resulted from multiple factors. It held that although the profit resulting from the combination of separate property and community labor must be apportioned according to the contribution, the property itself took its character as separate or community when acquired and retained that character even if there was a subsequent marriage. The residence thus remained the husband's separate property, and the wife's interest was not one of title. The community was, however, entitled to share in the enhanced value of the property that resulted from the expenditure of community funds and labor. The court stated that the amount could be based on the amount of community funds spent (i.e., reimbursement) or on the value of the property at the dissolution of the marriage. For real estate cases, the court decided that the value at dissolution was the appropriate formula. *See also Lawson v. Ridgeway*, 233 P.2d 459 (Ariz. 1951).

The approach used by the Arizona court permits equity at dissolution. In Wisconsin, equity at dissolution is obtained under the statute providing for equitable division of property at dissolution. Wis. Stat. § 767.61. The Arizona approach is inadequate during marriage because the asset is not reclassified as marital property. If the approach were adopted in Wisconsin, the nontitled spouse could not use the asset to obtain credit nor would the statutory remedies be available. The Arizona approach is also inadequate at the death of the nonowning spouse because all the property remains the separate property of the surviving spouse and is not subject to testamentary disposition.

California, like Arizona, permits the community to share in the appreciation of an asset in proportion to the amount the community expends to reduce the indebtedness. California accomplishes this by reclassifying the asset and thus avoids the problems in *Honnas*. The leading case is *Moore v. Moore*, 618 P.2d 208 (Cal. 1980). In that case, the wife, before marriage, purchased a house for \$56,640.57, paying \$16,640.57 as a down payment. The credit balance was secured by a mortgage on the house. Before marriage, the wife made seven payments on the loan principal, thereby lowering the balance due by \$245.18. During the marriage, community funds were used to make the mortgage payments, reducing the principal balance by \$5,986.20. At the time of the trial, the house had a value of \$160,000, and the couple's equity therein was \$126,812.45.

In deciding the case, the court noted that when community funds are used to make payments on property purchased by one of the spouses before marriage, the community receives a pro tanto community property interest in such property in the ratio that the payments on the purchase price with community funds bear to the payments made with separate funds. This rule excludes the portion of payments for interest and taxes. The spouse is entitled to share in the increase in fair market value of the property rather than only obtaining reimbursement. The court also noted that decisions in other community property jurisdictions (Arizona, Idaho and Washington) are in accord. *Hanrahan v. Sims*, 512 P.2d 617 (Ariz. Ct. App. 1973); *Gapsch v. Gapsch*, 277 P.2d 278, 283 (Idaho 1954); *Merkel v. Merkel*, 234 P.2d 857, 864 (Wash. 1951); *Drahos v. Rens*, 717 P.2d 927 (Ariz. Ct. App. 1985); see *Washington Deskbook*, *supra* § 3.20.

In *Moore*, the loan was made before marriage and thus was a separate property contribution. The court computed the separate property percentage interest in the home. This was the amount of the down



payment (\$16,640.57) plus the full amount of the loan (\$40,000), reduced by the amount of the loan paid from community property (\$5,986.20). This left a total separate contribution to the purchase of \$50,654.37. This sum, divided by the purchase price, yielded a separate property share of 89.43%. The separate property was thus 89.43% multiplied by the \$103,359.43 of appreciation in the property plus the down payment and principal reductions made by separate funds.

The community property percentage was found by dividing the amount of mortgage payments made with community property (\$5,986.20) by the purchase price, producing a community interest of 10.57%. That percentage multiplied by the \$103,359.43 of appreciation was added to the amount paid by community funds to give a total community share of \$16,911.29. The community amount was then divided between the spouses.

In *In re Geise*, 132 B.R. 908, the wife purchased a residence for \$50,000. She made a \$9,100 down payment from her individual property and borrowed the balance on a mortgage note. During the marriage, the wife's marital property wages were used to make the mortgage payments. On the date that the husband filed for bankruptcy, the mortgage note's principal balance had been reduced to \$40,640.

At the time that the petition was filed, the home had appreciated in value by \$3,120. In determining what portion of the residence was marital property, the court adopted the formula used in *Moore*. Thus, the bankruptcy estate was entitled to all marital property owned by the parties, namely the \$260 reduction in the mortgage balance during the marriage and a share in the appreciation of the residence determined by the marital property investment in the house. Of the total value of the home, .52% of the appreciation realized before filing of the bankruptcy petition was also part of the bankruptcy estate. The court concluded that the reduction of the note's principal balance and share of the appreciation was de minimis and found that the entire residence had retained its individual property classification and was not part of the husband's bankruptcy estate.

The decision in *Moore* was followed in *Marsden*, 181 Cal. Rptr. 910. In *Marsden*, however, an additional fact was that the husband had owned the property for nine years before marriage and the home's value had appreciated during those nine years. The court held that the husband should have the benefit of the prenuptial appreciation and added the

prenuptial appreciation into the *Moore* formula as a separate contribution. *See also Dorbin v. Dorbin*, 731 P.2d 959 (N.M. Ct. App. 1986).

Washington has adopted a similar approach. *Elam v. Elam*, 650 P.2d 213 (Wash. 1982). New Mexico also reaches a similar result through a theory of doing substantial justice. *Portillo v. Shappie*, 636 P.2d 878 (N.M. 1981). Wisconsin likely will adopt the California approach.

Classifying an asset in cases in which both spouses have died and there is no evidence as to what money was used to reduce the indebtedness on a spouse's separate property raises the need for presumptions, because the classification of the funds expended during the marriage must be determined. Most states presume that separately owned funds, if available, were spent to reduce a debt on separate property. *Suter v. Suter*, 546 P.2d 1169 (Idaho 1976); Reppy & Samuel, *supra* § 3.12, at 109. This presumption applies to mortgage payments made during the marriage. However, in California the rule is that no presumption exists, and in Arizona it is presumed that community funds were used to pay off a mortgage on separate property, but that separate funds were used to build a house on separate land. *Sommerfield v. Sommerfield*, 592 P.2d 771 (Ariz. 1979); *Seligman v. Seligman*, 259 P. 984 (Cal. Ct. App. 1927). Wisconsin is likely to follow the majority and presume that separately owned funds were spent to reduce a debt on separate property, because this result is consistent with the presumptions in the family-expense doctrine. *See supra* § 3.20.

### **3. Improvements [§ 3.42]**

Once it is determined that there is no gift, if an asset has been physically improved using funds of a different classification the issue is whether the improvement retains the classification of the original property or whether a mixed asset is created. *See Washington Deskbook, supra* § 3.20 (discussion of issues when property of one classification is improved using funds or labor of a different classification). Most state decisions follow the fixtures doctrine, whereby the improving estate is entitled to reimbursement of the amount expended but the improved asset retains its original classification. *See* Reppy & Samuel, *supra* § 3.12, at 106; *see also Rogers v. Rogers*, 754 S.W.2d 236 (Tex. Ct. App. 1988); *Potthoff v. Potthoff*, 627 P.2d 708 (Ariz. Ct. App. 1981). If the expenditures relate merely to the maintenance of the property and do not

add to its value, no reclassification occurs. See *In re Czerneski*, 330 B.R. 240 (Bankr. E.D. Wis. 2005), which held that the payment of real estate taxes on a vacant lot classified as individual property using marital property funds only maintained the property and, thus, did not create a marital property interest in the property. The other community property states are divided on whether reimbursement should be ordered. Reppy & Samuel, *supra* § 3.12, at 107. For example, should lawn-service expenses be reimbursed? It has been held that community property funds can be used to paint and repair a separate rental duplex when the rental income is classified as community property. *Bridges v. Osborne*, 525 So. 2d 337 (La. Ct. App. 1988).

A small minority of California cases reject the fixtures doctrine and hold that the improving estate owns the improvement. Thus, in these cases, if the spouse uses community funds to build a house on his or her separate land, that spouse would continue to hold the land as separate property but the community would own the house. *Id.* This approach is consistent with the ownership preference of the Act. It is also consistent with the result when an asset is improved through substantial undercompensated labor. Wis. Stat. § 766.63(2). As a general rule, however, this approach is more difficult to apply than the fixtures doctrine because expenditures for a new roof or kitchen remodeling create ownership interests that are difficult to separate or measure.

A third alternative for dealing with physical improvements was set forth in *Sparks v. Sparks*, 158 Cal. Rptr. 638 (Ct. App. 1979). In that case, a house was built on community property with the wife's separate funds, and no gift was intended. The house represented the principal value of the property. The court held that it would be unfair to apply the fixtures doctrine and instead allowed the wife's separate estate to buy into the present fair market value of the house and land in the ratio that the original cost of the house had to the value of the land at the time of construction.

If the fixtures doctrine is followed, it is necessary to determine the amount of reimbursement. In some states, no reimbursement is permitted when separate funds are used to improve community property absent an agreement for such reimbursement. *Fabian v. Fabian*, 715 P.2d 253 (Cal. 1986). The issue is whether the reimbursement should always be for the amount expended or should be limited to the enhanced value of the property if this is less. In many decisions, the enhanced value of the property has been used as a limit on the amount of

reimbursement. *See, e.g., Bazile v. Bazile*, 465 S.W.2d 181 (Tex. Ct. App. 1971) (writ dismissed w.o.j.). In *Warren*, 104 Cal. Rptr. 860, however, the larger amount was reimbursed. *See supra* § 3.40. In situations in which community funds are used to bring a separate mineral estate into production, reimbursement is limited to the amount spent. Reppy & Samuel, *supra* § 3.12, at 107.

In Louisiana, reimbursement is the amount expended regardless of the enhancement of value. La. Civ. Code arts. 2364–67 (West, WESTLAW current through the 2009 regular session). This is similar to an interest-free loan, and this rule makes sense when the property improved is earning income that is community property (as in Wisconsin) or when the family is occupying the property or deriving some other benefit from it. The community does not, however, share the appreciation. Under this approach, reimbursement can include amounts spent for real estate taxes, interest, and routine maintenance. It is inconsistent, however, with the *Moore* approach. *See supra* § 3.41.

Idaho, which has the same income rule as Louisiana and Wisconsin, usually measures reimbursement by the enhanced value at dissolution. *Hiatt v. Hiatt*, 487 P.2d 1121 (Idaho 1971). This generally ensures equity for the community because the income is community property and the enhanced-value test allows the capture of a share of unrealized capital gain. In Texas, which also follows the rule, reimbursement is deemed an equitable claim and community expenditures must exceed community benefits before reimbursement is ordered. Community benefits include occupancy, income, and income tax deductions. Occupancy is offset against the community claim for reimbursement for taxes, insurance, and interest paid on separate property but not against a community reimbursement claim for reduction of indebtedness on separate property. *Hawkins v. Hawkins*, 612 S.W.2d 683 (Tex. Ct. App. 1981); *see also* Reppy & Samuel, *supra* § 3.12, at 108–09.

### **G. Assertion of Mixing Rules by Creditor [§ 3.43]**

The final question in connection with mixing property having different classifications is whether a creditor may take advantage of a spouse's right to reimbursement or obtain an ownership interest in property titled in the name of the other spouse. In most of the other community property jurisdictions, spouses—and therefore their creditors—must await termination of the community to assert

reimbursement and ownership claims. Reppy & Samuel, *supra* § 3.12, at 109. In California, this rule is followed unless the community estate is left insolvent when the contribution to the separate estate is made. In Washington, however, the court in *Conley v. Moe*, 110 P.2d 172 (Wash. 1941), permitted a creditor who was entitled to collect from the community to seize the community's claim to reimbursement during the existence of the community.

In Wisconsin, there is no time restriction for asserting the mixing rule, and normally the spouse will have acquired an ownership interest in the property. It is marital property that the spouse may use to obtain credit and that is subject to the remedies provisions during marriage. As such, it appears that a creditor may use the mixing statute during marriage to satisfy an obligation incurred in the interest of the marriage or the family.

## **H. Appreciation through Labor [§ 3.44]**

### **1. General Rules [§ 3.45]**

In addition to mixing by the use of marital funds, a second type of mixing occurs when a spouse applies labor to the property, other than marital property, of either spouse. Under the Act, substantial labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity applied to either spouse's property other than marital property creates marital property attributable to that application if reasonable compensation was not received and substantial appreciation results from the application. Wis. Stat. § 766.63(2).

The statute does not organize the analysis of whether labor has created marital property. However, it seems appropriate to consider first whether substantial labor was applied. The comment to section 14 of UMPA states that the rule is strict and has a bias against the creation of marital property from personal effort, unless the effort is substantial. As the comment explains, "Routine, normal, and usual effort is not substantial." The comment states that "[r]eal property transactions are those in which the problem will typically occur. This might be work on a farm, or improvements or additions to a home or to a piece of commercial real estate." The substantial effort requirement of the Act is not easy to apply. For example, if a spouse puts a new roof on an inherited cottage, it is an improvement to the asset. Is this substantial labor? If a spouse builds an addition to the cottage, is this substantial

labor? What, by contrast, is routine, normal labor? Is it limited to regularly recurring maintenance? The Act provides no answer; however, labor that constitutes only recurring maintenance should not create marital property. In *Josephson v. Josephson*, 772 P.2d 1236 (Idaho Ct. App. 1989), the court held that labor expended to remodel the interior of a residence, construct a patio, and landscape the property at a cost of \$20,000 did not enhance the value of the property; thus, no reimbursement was appropriate.

The Act attempts to avoid the valuation of all labor expended by requiring that substantial labor be involved to create marital property. Thus, if a spouse spends time working on a hobby, such as an inherited coin collection, it is possible that all the appreciation realized will be individual property. If the spouse, however, devotes too much time and effort to buying and selling the coins, that activity may be sufficient to become a business in itself, and the appreciation may then be marital property. If a spouse spends a substantial amount of time subdividing separate land, that may put the spouse in the real estate business and transform the appreciation on the land to community property. *Hiatt v. Hiatt*, 487 P.2d 1121 (Idaho 1971); *Evans v. Evans*, 453 P.2d 560 (Idaho 1969).

The question of substantial labor is not limited to physical labor; it also arises with intellectual activity. If a spouse is employed full time in one occupation and devotes one hour per day to following his or her inherited securities, is this substantial labor? If the spouse had no other employment and spent six hours per day on the inherited securities, would this be substantial? Would it depend on what the spouse did during that time? Would it depend on whether security transactions were made based on the analysis? Note that in the physical labor examples, there was a substantial amount of time expended over a short period. In the intellectual labor example above, less time was expended in the short period, but the labor extended over an indefinite period. In all cases in which a spouse devotes a significant amount of time to an asset that is classified as other than marital property, there is the possibility that the labor will be deemed substantial and will invoke the mixing rule.

If substantial labor was expended, the second inquiry concerns whether reasonable compensation was received. Normally, no monetary compensation is paid when labor is expended for home improvements or for management of personal investments or a farm operation. Any monetary compensation in those circumstances would have to be paid

from the individual property or predetermination date property of the spouse benefiting from the labor. It appears that only monetary compensation is considered; it is unlikely that a family's use of the improved cottage in the above example will be considered compensation and the fair market value of such use analyzed to determine if it is reasonable compensation. The comment to UMPA section 14 refers to compensation paid, which implies monetary compensation. Typically, reasonable compensation is only a factor in the operation of a business; business situations are discussed below. For an analysis of income retained in a partnership, see *Todd v. Commissioner*, 153 F.2d 553 (9th Cir. 1945).

If there was no reasonable compensation, the final inquiry is whether the labor caused the property to substantially appreciate. UMPA does not explain what constitutes substantial appreciation. Nevertheless, it is unlikely that putting a new roof on an inherited cottage constitutes substantial appreciation. On the other hand, the comment to section 14 of UMPA indicates that an addition to a home may cause substantial appreciation of the property.

When physical labor is expended over a short period, the value of the asset before and after the labor is expended should be the measure for substantial appreciation. The inquiry under the Act appears to be the enhanced value or the extent the asset has appreciated, not the cost of having the labor performed by a third person.

In situations in which the labor is expended over an indefinite period, however, determining what is substantial entails more than merely comparing of the value at the time of litigation to the value before the labor commenced. For example, if security investments, followed over a period of years, increase in value from \$10,000 to \$30,000, this is not necessarily substantial appreciation. The investments' appreciation must be compared with the change in published market averages. If the increase in value is similar to market averages for securities for which no trading has occurred, the appreciation is not attributable to the labor.

When the increase in value is substantial and attributable to substantial undercompensated labor, the Act provides that the labor creates marital property. If in the example above, the market averages had increased 40%, so that the natural growth would have been from \$10,000 to \$14,000, would the marital property be \$16,000 or \$20,000 (\$30,000 less \$14,000 or less \$10,000)? The marital property interest

would only be the additional value attributable to the substantial labor, i.e., \$16,000.

The cases in this area have primarily involved business interests and are often connected with questions involving the income from such property. States (like Wisconsin) in which income on separate property is community property—Texas, Louisiana, and Idaho—have a civil-law system based on Spanish law. Under the American rule of the other community property states, income on separate property is separate property. Many of the decisions involving labor by a spouse from those states are affected by the different treatment of income on separate property. In particular, some of the remedies are inappropriate in Wisconsin because the income in Wisconsin is already marital property. The development of two different approaches for allocating appreciation in the value of an individual property business resulting from labor by a spouse during marriage is considered in J. Thomas Oldham, *Separate Property Businesses That Increase in Value During Marriage*, 1990 Wis. L. Rev. 585.

In the following cases involving business interests, the spouse worked in the business and generally was found to have performed substantial labor. Unless otherwise indicated, the business had also appreciated in value.

## **2. Sole Proprietorship [§ 3.46]**

Cases involving a sole proprietorship differ from cases involving other business entities because the business assets of the sole proprietorship are owned by a spouse and not by the entity. Thus, if a spouse performs substantial undercompensated labor, the mixing statute is applied, and it applies to the business assets in the same manner it applies to labor on a residence or investment portfolio. In the reported cases, the compensation issue is not addressed. Under the Act, however, if the amount withdrawn from the business as compensation is reasonable, the appreciation in the business is not marital property. Wis. Stat. § 766.63(2). If the income of the business is retained and used for business purposes, the assets acquired with those funds are marital property. Wis. Stat. § 766.63(1).

The general rules on appreciation resulting from labor of a sole proprietorship are set forth in *Abraham v. Abraham*, 87 So. 2d 735 (La.



1956). At the time of marriage, the wife owned as her separate property a controlling interest in an unincorporated business. She operated the business as general manager, credit manager, cashier, and chief salesperson. In the eight years the parties were married, the business tripled in value. Based on a Louisiana statute, the court held that if during the marriage either spouse substantially contributed to the increase in the value of the separate property of one spouse, the nonowning spouse was entitled to one-half the value of the increase. Substantial community labor had occurred, and the separate property had increased in value. Once this was established, the burden of proof shifted to the wife to affirmatively establish that the increase in value resulted from independent factors, such as inflation, chances of trade, and the ordinary course of events. In *Abraham*, the court determined that the only testimony to that effect was self-serving and therefore was insufficient; the court held that the increase in value was community property.

*Lopez v. Lopez*, 113 Cal. Rptr. 58 (Ct. App. 1974), concerned the classification of assets in a law partnership. The husband began a law practice in 1953 as a sole practitioner. From 1955 through September 1957 and on two occasions thereafter, he practiced in a partnership. The parties were married in August 1957. The husband's income increased substantially during the marriage. The issue was how to classify his interest in the law partnership and the proceeds he received when two partners were brought into the partnership. Classification was required because in California, only community property is divided in a divorce proceeding.

The court held that because the practice had become lucrative as a result of the husband's industry and professional ability during marriage, the business was a community property asset with substantial value. The primary value of the practice was derived from the husband's individual efforts after the marriage, rather than from the relatively negligible sum of money initially invested in the practice and the value attributable to periods before marriage. In this case, the value of the law practice "was clearly one and the same as the husband's energy, skill, judgment, intelligence and personality as a practicing attorney." *Id.* at 65.

*Lopez* differs from *Pereira*, *Van Camp*, and *Beam* because in those cases, the husbands' separate property played a key role in their businesses. In *Lopez*, the trial court may well have concluded that the "husband's initial investment in his law practice became so commingled

with the community that all traces and vestiges of it as separate property have been lost.” *Id.* at 66. The “professional goodwill may thus be separate property, community property, or varying degrees of both depending upon the particular circumstances. The fact that ‘professional goodwill’ may be elusive, intangible, difficult to evaluate and will ordinarily require special disposition, is not reason to ignore its existence in a proper case.” *Id.* at 67 (listing the factors in valuing goodwill).

A farm was at issue in *Cockrill v. Cockrill*, 601 P.2d 1334 (Ariz. 1979). At the time of marriage, the husband owned a farming operation as separate property. During the marriage, the net worth of the farm increased substantially. (In Wisconsin, it is appropriate to determine only the increase in value of the property itself and not the change in net worth of the business because net worth includes retained income, and all income—absent a unilateral statement—is marital property.) The trial court found that this increase was attributable primarily to the efforts of the husband and thus was community property. The husband appealed, claiming that the increase in net worth resulted primarily from the inherent nature of the separate property and was, therefore, also his separate property.

On appeal, the court first held that when the value of separate property has increased, the burden is on the spouse contending that the increase is separate to prove that the increase is because of the inherent value of the property itself and not the work effort of the spouse. The court then rejected its prior all-or-nothing rule and held that it would instead apportion the increase in value between the separate property and community property. The court found that all the community property states except Texas had rejected the all-or-nothing approach. (Texas has since changed its rule. *Vallone v. Vallone*, 644 S.W.2d 455 (Tex. 1982).)

According to the court, because there is no fixed standard for allocating appreciation, a court should use the yardstick most appropriate and equitable in a particular situation. The court stated that in the case of real estate, there were three possible approaches: (1) award the owner of the separate property its rental value, with the community entitled to the balance of the income produced from real estate by the parties’ labor, skill, and management; (2) determine the reasonable value of the community services and allocate that amount to the community, with the balance treated as separate property attributable to the inherent nature of the separate estate; or (3) simply allocate to the separate property a reasonable rate of return on the original capital investment, with any

increase above this amount considered community property. *See Potthoff*, 627 P.2d 708.

*Cockrill* is an Arizona decision, and the possible approaches reflect Arizona's rule that income on separate property is separate property. In states like Wisconsin, where income on separate property is community property, allocating the reasonable rental value to the separate property is inappropriate because this income is already marital property. Moreover, allocating the value of the labor to the community does not recognize the creation of an ownership interest and the failure to have paid reasonable compensation. *See* Wis. Stat. § 766.63(2). Thus, in Wisconsin, the first two *Cockrill* approaches are not appropriate. The only alternative from *Cockrill* that could be used in Wisconsin is allocating a reasonable rate of return on capital to the individual property, i.e., natural appreciation.

The court of appeals in *Haldemann v. Haldemann*, 145 Wis. 2d 296, 426 N.W.2d 107 (Ct. App. 1988), considered whether appreciation in the value of property resulting from a spouse's labor was divisible. The Haldemanns lived on a farm that the wife had inherited. During the marriage, the husband

assisted in planning and construction of a new sunroom, converted a former chicken coop into a two-car garage, planted trees, seeded the lawn, installed a water heater and softener, rewired parts of the residence, wired the barn, built hogpens, removed an old silo foundation, filled an old cistern, leveled dirt for cementing, removed an old chimney and closed the roof, insulated the house ceiling, relocated a window in a lower bedroom, paneled walls, laid carpet in the second bedroom, installed a stairway iron railing, installed gutters and downspouts, built an insulated wall on one side of the house, constructed a base for a TV tower, planted trees to prevent soil erosion, removed an old porch and asbestos siding, backfilled around the garage, and constructed a dry well for roof drainage.

*Id.* at 306. The issue in the divorce action was whether these services constituted normal home repairs and maintenance or whether they constituted improvements resulting from the husband's labor. If they were improvements resulting from the husband's labor and the improvements increased the value of the property, then the increase in value would be divisible. (Note that this test is different from the requirement in section 766.63(2) in which "substantial" labor is required to classify appreciation on individual property as marital property.)

The parties' experts testified that the value of the Haldemanns' farm property had increased during the marriage by 5 to 40 percent and that the value of other farm properties during that period declined, some by as much as 50 percent. The record did not indicate that the increase in value was attributable to any unique features of the farm or its surroundings. Still, the circuit court refused to find that the husband's labor had caused the value of the property to increase, thereby denying that the increase was subject to property division.

The appellate court reversed. The court held that appreciation in the value of inherited property resulting from the efforts and abilities of the nonowning spouse is part of the property that is divisible in a divorce. The court agreed that the nonowning spouse's efforts and abilities must be unusual and uncompensated to the extent that they require something more than the performance of usual and normal marital responsibilities. It is not necessary, however, that the nonowning spouse's efforts and abilities be beyond or apart from the owning spouse's efforts and abilities. On the other hand, merely maintaining the marital relationship and performing the customary obligations of one spouse to the other does not constitute a contribution by the nonowning spouse that requires that the appreciation in value of the inherited property be treated as part of the divisible property.

The wife argued that the husband had operated a hog-raising business during the marriage and that the income from this business had compensated the husband for his efforts and abilities. (For marital property mixing rules to apply, there must not have been reasonable compensation.) The husband was not charged rent for the use of the farm property for this business. The court found that the parties had jointly operated and benefited from the hog-raising business and therefore rejected the wife's argument that the husband had been compensated. The court also held that it was irrelevant that the wife had paid for the materials and supplies that went into the improvement of the farm and its buildings. The husband's claim also was not affected by the fact that some of his efforts were used to make the farm suitable for a hog-raising operation. This conclusion was reached because those efforts increased the value of the farm and the farm buildings. Thus, the court held that the husband's efforts and abilities had increased the value of the farm and the farm buildings and that this increase was part of the divisible estate in the divorce proceeding.

Similarly, in *Krejci v. Krejci*, 2003 WI App 160, 266 Wis. 2d 284, 667 N.W.2d 780, the husband inherited a resort property before the marriage. The resort at the date of marriage was subject to a balance due on a land contract. During the marriage, the parties built a large addition to the main house, including five bedrooms, a bath, and a living area. The husband did much of the labor himself, and he managed the resort full time. The land contract payments were made in part from resort operation income with a final balance satisfied with funds he inherited. The wife worked in a nursing home from the fall to the spring of each year. From May through September, she helped run the resort. She was assisted by her children from a prior marriage. Neither the wife nor the children were compensated for their labor. At the time of the marriage, the property tax statement showed that the resort had a value of \$151,000. At the time of divorce, the market value was \$398,000. There was no expert testimony introduced to establish the appreciation attributable to the increase in value of the land itself during the marriage.

The court of appeals found it undisputed that income from the resort was used in part to build the addition to the marital home, make other improvements to the resort property, and pay a portion of the land-contract payments. As a result, marital property was invested in the inherited resort. The court also found that the improvements to the residence were significant. The addition, as well as the new septic systems, well, and sea wall, were more than routine upkeep of the property. The court held that the husband's and wife's income and labor were invested in the resort. The evidence introduced failed to demonstrate how to specifically trace and identify their added investment. Thus the court held that the appreciation was part of the marital estate and, accordingly, divisible by the circuit court.

A similar analysis was made in *Applegate v. Applegate*, 365 N.W.2d 394 (Neb. 1985), to determine if an asset retained its inherited status. In that case the wife's contributions were considered "typical of a wife of a farmer-cattle raiser." *Id.* at 397. The contribution included help "with branding, dehorning, calving, sorting out, feeding, weed burning, irrigation, fencing, putting up hay, and resetting irrigation pipe." *Id.* These services were held not to contribute directly to any preservation of or increase in the value of the property. However, the funds and labor expended to add a new addition to the residence were significant and made part of the inherited parcel divisible.

A somewhat different issue was raised in *Denney v. Denney*, 171 Cal. Rptr. 440 (Ct. App. 1981). The husband owned and operated a doughnut shop that was his separate property at the date of marriage. During the marriage, he became an alcoholic and the business became almost worthless. The wife took over the operation, and before their separation, the business recovered most of its initial value. During the marriage, the spouses had withdrawn funds from the business to cover their living expenses. The wife asserted that the increased value of the business from her labor was community property.

The court held that when the value at separation is no greater than the value at the date of marriage, no community interest is acquired. A court cannot be expected to value a business at numerous times during the marriage. The only exception to this rule is in a situation in which a bankruptcy has occurred so that a date has been fixed at which the business had no value. *Winn v. Winn*, 159 Cal. Rptr. 554 (Ct. App. 1979).

In Wisconsin, if reasonable compensation is not received, the appreciation attributable to substantial spousal labor is marital property. The result is consistent with *Abraham*. Wisconsin courts also are likely to reach the same result as that reached by the court in *Denney* because substantial measurable appreciation did not occur. In some states, the community receives only what would be reasonable compensation for the labor performed. This result is inconsistent with the Act, which states that marital property is created. Wis. Stat. § 766.63(2).

In *Schorer v. Schorer*, 177 Wis. 2d 387, 501 N.W.2d 916 (Ct. App. 1993), the husband had inherited stock in a closely held business from his father. The stock appreciated during the marriage, and the issue was whether any portion of the value was included in the divisible estate. The circuit court held that the entire interest in the business was divisible, basing its determination on the fact that the business was in bankruptcy in the early 1980s during the marriage and had only minimal value at that time. Therefore, all the value of the business was generated during the marriage and was not the result of the inheritance. In addition, all of the appreciation in the business resulted from the spouses' efforts (primarily the husband's). The court held that the value of the business was divisible even though the husband had received adequate compensation for his efforts during the marriage. *See supra* § 2.51. This result is different from the classification rules under chapter 766, which do not classify appreciation in the value of individual property resulting

from efforts of a spouse as marital property if reasonable compensation is received. Wis. Stat. § 766.63(2).

### **3. Incorporated Business [§ 3.47]**

In all the community property states, the spouse asserting an apportionment of a business interest has the burden of proving that the value of the business has increased as a result of a spouse's labor. If this is not done, there will be nothing to apportion. Once this threshold issue has been met, the next step is to see whether reasonable compensation was received. When a spouse receives a salary for services to the company, that salary is presumed to be adequate compensation for the services rendered, and the other spouse must show that the salary was unreasonable. If the services were irregular, the other spouse must prove they had extreme value. The entire principle of apportionment is based on a substantial community contribution to the assets. In most cases in which an apportionment has been made, one spouse has been in control of the business and able to set his or her own salary and determine the business's dividend policy. A spouse in such a position is able to manipulate his or her income and enhance his or her separate property while exercising management and control over both separate property and community property. *See Weekley, Appreciation of a Closely-Held Business Interest Owned Prior to Marriage—Is It Separate or Community Property*, Comm. Law J. 261 (Fall 1980).

The significance of a majority interest in an incorporated business is that a spouse with majority interest can, acting alone, declare dividends and disburse the corporate earnings or retain those earnings. In addition, the spouse with control of a corporation can liquidate the corporation and obtain direct ownership of the appreciated assets. This is not possible if the spouse has a minority interest in a corporation. In the unincorporated business previously discussed, all the business income was marital property and, if retained in the business, caused the business assets themselves to become marital property. The obligation of good faith in the Act expressly provides that a spouse is not obligated to produce income on his or her nonmarital property. Wis. Stat. § 766.15(2). In the cases discussed below, the corporation has earned income and has retained a portion of it. One spouse was employed by the business and performed substantial labor. Following the suggested approach, once substantial labor is established the next question is whether reasonable compensation was received for such services.

The court addressed the issue of what constitutes reasonable compensation in *Speer v. Quinlan*, 525 P.2d 314 (Idaho 1973). The husband started working in his father's company after his marriage, became a co-manager of the business, and later received 320 of the 500 total shares of the business stock. From the time the husband began working in the company through the date of divorce, the corporation's market value more than tripled. The company never declared any dividends and had several hundred thousand dollars of undistributed after-tax earnings. The husband, who devoted much time to the job, had received compensation in the form of a salary, bonuses, and fringe benefits during the entire term of his employment. The wife also made some contributions to the business through entertaining business guests, but she received no compensation from the company.

The court held that if community efforts have been expended in the conduct of a separate property business, a proper inquiry upon dissolution is whether the community has received fair and adequate compensation for its labor. The court further held that a trial court should take into consideration the nature of the business, the size of the business, the number of employees, the nature and extent of community involvement in the conduct of the business, and the growth pattern of the business. Once those questions have been answered, the proper inquiry is whether the overall compensation the community received was equivalent to the compensation the business would have had to pay a nonowner employee to perform the same services rendered by the spouse. This involves analyzing the salaries of nonowner employees at the same level of responsibility in comparable businesses in the same area of the country. In Idaho, if the compensation is not reasonable, a judgment for the amount of such compensation is awarded.

In Idaho, after it is determined whether reasonable compensation was received and a judgment rendered if required to provide a reasonable compensation, the court considers whether the accumulated net after-tax earnings of the company are properly deemed to be community property and thus divisible at divorce. In Wisconsin, this may occur in situations in which inadequate compensation has been paid. The issue in Wisconsin is whether the nonemployee spouse receives an ownership interest in the stock or a share of the corporate income, including the retained income. No contention was made in *Speer* that the retention of the net earnings was unreasonable from a business point of view or that they were retained to defraud the community. The question was whether the retained earnings constituted income that was a community asset



subject to division under Idaho law. The court initially held that the retention of the earnings in the business did not present a case of community funds being invested in a separate property business and thus that no ownership interest in the business was community property. However, the court did hold that under the discretionary-division-at-divorce statute applicable in Idaho, any inequity that the retention of income may have caused could be rectified. This decision gives the nonowner spouse the right to participate in the corporate income that is accumulated during the marriage.

Texas also has considered whether substantial appreciation of the corporation is classified as individual property when a spouse with majority interest in a corporation receives a reasonable salary. *Vallone v. Vallone*, 644 S.W.2d 455 (Tex. 1982), is relevant in Wisconsin in cases in which inadequate compensation was paid. The husband worked in his father's restaurant. During the marriage, the assets of the restaurant, a sole proprietorship, were transferred to the husband as a gift and became his separate property. When the husband incorporated the business, 47% of the initial capitalization was traceable to the separate property received by gift from the father, and the balance was community property.

During the marriage, the business prospered and the husband received a salary and bonus of approximately \$200,000 per year. At the time of the divorce, the business was worth \$1 million. Of this amount, testimony indicated that \$700,000 was attributable to retained earnings, and it was agreed that there was no natural increase in the value of the separate property. The trial court held that 47% of the initial capitalization was traceable to the husband's separate estate, and it therefore set aside 47% of the corporate stock as his separate property. The court of appeals reversed and held that the separate property had substantially increased by reason of community labor and that the division of the estate was therefore manifestly unfair.

In a 5–4 decision, the Texas Supreme Court held that the 47% interest was properly classified as separate property, but that this holding did not preclude a right of reimbursement. (In Wisconsin, the payment of reasonable compensation precludes further inquiry.) The court found that a spouse may spend a reasonable amount of talent or labor in the management and preservation of his or her separate estate without impressing a community character upon that estate. *See Jensen v.*

*Jensen*, 665 S.W.2d 107 (Tex. 1984) (analyzing reimbursement theory and ownership theory for compensating labor by a spouse).

The decision in *Vallone* summarizes the formulated rules in other community property states when reimbursement is sought for uncompensated community labors. The decision states that Washington follows the rule that when a closely held corporation pays a salary to a spouse, it is presumed that the community has been compensated for the spouse's services, and the enhanced value retains its separate character. In Arizona, the spouse's salary must be fair and adequate, otherwise the entire increment in value is deemed community property. California applies either of two rules: under one rule, the court allocates a reasonable rate of return on the separate property to the separate estate and apportions the remainder to community and under the other rule, the court awards a reasonable value for the spouse's services to the community. Nevada applies both California tests. New Mexico reimburses or allocates to the community the reasonable value of the spouse's labor. Idaho courts are in accord with New Mexico and consider several factors when determining if the salary paid to the spouse is fair compensation for the labor expended. The factors considered include the nature and size of the incorporated business, the number of employees, the extent of the spouse's involvement, and the growth pattern of the business. If the spouse has not received or taken adequate compensation from the corporation, the courts will award the community the difference between the compensation received and what the corporation would have had to pay an employee to perform the same services.

The Idaho court considered a minority shareholder in *Simplot v. Simplot*, 526 P.2d 844 (Idaho 1974). When the marriage took place, the husband owned shares in a holding company, which in turn owned shares in an operating company. The combination of the shares gave the husband an 8.4% interest in the operating company. He was a director of the holding company and was employed as an officer of the operating company. During the marriage, the operating company's retained earnings increased dramatically. The husband's 8.4% interest in these earnings was several million dollars, which the wife claimed was community property to be divided at divorce.

The first issue was whether the increase in value of the stock as a result of the retained earnings was income (community property) or natural enhancement of the property (separate property). The court noted

that the husband, as a minority shareholder, could not have caused dividends to be declared or caused the directors to reinvest the earnings. Therefore, the court held that the increase in retained earnings was natural enhancement and not income, rents, or profits.

The second issue was whether the increase in retained earnings resulted from community labor. The court considered whether the husband had brought any special skills to the job, as well as the level of compensation he received during his employment. There was no evidence that the husband's salary was inadequate in light of his responsibilities, and there was no evidence that the corporate structure was set up to deprive the community of these earnings. The court held that the husband's efforts during the marriage had not contributed to any increase in the value of the company assets or stock. The decision not to recognize the increased corporate value is directly opposite in result to the decision in *Speer* and can only be explained by the difference in the spouse's ownership interest—majority versus minority—during the marriage.

In Idaho, where *Speer* and *Simplot* arose, there are two questions in cases in which labor is performed by a spouse as a corporate employee and the spouse holds stock in the corporation initially as separate property. The first is whether the compensation received during the marriage is adequate. The second is what sum earned by the company should be considered rents and profits resulting from the labor of a spouse (i.e., a return on capital) and thus divisible after deducting the reasonable compensation.

As to the second question, it is necessary either to allocate a sum to rents and profits, leaving the balance to represent a natural increase in value (which would be separate property), or to first determine the sum that is the natural increase in value, leaving the balance as rents and profits. Under the latter approach, it is appropriate to look first to published inflation indices and outside evidence of unusual market factors that could have caused a natural gain.

In divorce cases, Idaho courts have considered the increase during marriage in the value of a corporate business as a result of retained earnings. In Wisconsin, this is possible under section 767.61. However, in neither *Speer* nor *Simplot* did the Idaho court find that the accumulated corporate income itself was a community asset. Thus, the nonowner spouse could not have willed his or her one-half interest in the

corporation, and at the death of the owner spouse, a gift of the shares of stock would also transfer all interest of the nonowner spouse. It may be impossible in community property states to avoid this result in situations involving corporations.

The rules for a partnership are different from those for an incorporated business. In *Swope v. Swope*, 739 P.2d 273 (Idaho 1987), the husband owned an undivided one-quarter interest in a partnership before his marriage. The partnership owned both real and personal property associated with the operation of a business. During the marriage, the partnership retained earnings attributable to the husband's share of \$75,765, and the husband and the other partners created a corporation to which they transferred the personal property of the partnership. The husband received 4,000 shares of common stock and a \$100,000 debenture in exchange for his interest. The securities and the real estate, which continued to be held in the partnership, were later sold to a third party for \$840,000 during the marriage. The issue was the classification of these funds. In Idaho, income on separate property is community property.

The court found that a corporation is a separate legal entity distinct from its shareholders, while a partnership is instead the sum of the owners' interests. The court found fundamental ownership and control differences between partnerships and corporations. A partner has a right to direct the payment of earnings or, if the other partners disagree, to dissolve the partnership. A shareholder has no equivalent right. Likewise, shareholders are not corporate agents and do not make business decisions, while partners are agents of the partnership and have a right to make business decisions. "A partnership, then, is a contract of mutual agency, where each partner acts as a principal in his own behalf and as an agent for his co-partners, while the corporation is a separate and distinct entity, apart from the owners." *Swope*, 739 P.2d at 280. Thus, the court held that the earnings of a separate property partnership, whether retained or distributed, are community property.

The next issue was the effect on the stock's classification of the transfer of the retained earnings, as well as all other personal property, to the corporation. The husband performed no services for the corporation. The court held that the community had an interest in the corporation and that the wife was entitled to be reimbursed for the improvement or enhancement attributable to the contributions of the retained earnings to the corporation. The appellate court remanded the case for the trial court

to determine whether the value of the stock had increased during the period before the sale to the third party.

The Wisconsin Court of Appeals considered appreciation in the value of a corporation as a result of retained earnings for purposes of a property division in *Lendman v. Lendman*, 157 Wis. 2d 606, 460 N.W.2d 781 (Ct. App. 1990). In this case, the husband used \$8,500 of inherited funds to purchase stock in a corporation he created. The corporation used those funds plus borrowed funds to purchase a funeral home at which the husband was then employed during the marriage. Before the divorce action, the unpaid balance on the corporate obligation relating to the purchase of the business was reduced by approximately \$130,000. It appears that the parties agreed that the value of the stock had increased as much as the debt had been reduced. The parties agreed that the husband's labors created the corporate income that had paid for the retirement of the debt. It does not appear that there was a determination in the proceeding of the fair-market value of the business at the time of the divorce. The circuit court held that the appreciation in the value of the stock was inherited property and therefore not divisible.

The court of appeals initially determined that whether appreciation in an asset is divisible depends on whether the appreciation was "purchased with funds acquired" by inheritance as provided in section 767.255 (now section 767.61). The court did not discuss *Plachta*, 118 Wis. 2d 329, in which a different appellate court had held that natural appreciation is excluded from division. Likewise, the court did not use the analytical rule in the Act that there be substantial appreciation caused by substantial undercompensated efforts before the appreciation on individual property assets is classified as marital property.

The appellate court held the appreciation was not purchased with inherited funds, but rather was

paid for by corporate "income" generated through [the husband's] labors. In this regard, *Arneson* controls. In that case, we viewed income generated by an inherited asset as separate and distinct from the asset itself....

Here, the money used to pay off the corporate debt was earned income. Thus, just as in *Arneson* where property purchased by dividend income of an inherited stock was held to be marital, the appreciation purchased by earned income of a corporation acquired by inherited funds is also marital.

*Lendman*, 157 Wis. 2d at 612. The court did not note the distinction that income on securities is received by a shareholder when dividends are paid by the corporation, not when the corporation generates the income. The court's holding apparently would be the same regardless whether the corporate income was used to reduce acquisition debt or used for other corporate purposes, such as expansion of facilities.

In the portion of its decision dealing with property division, the court did not consider the amount of compensation taken by the husband. However, the decision includes a review of the maintenance determination. In that section, the court noted that the husband's annual salary had declined by more than \$10,000 for the last two years. During that two-year period, the corporation's retained earnings increased from \$12,000 to \$60,000. The circuit court had found that the husband's self-imposed salary cuts were bogus. The appellate court did not discuss or challenge that finding. The circuit court increased the husband's salary for maintenance purposes to the level before the reduction.

This decision can be reconciled with the divorce decisions in other community property states in which the husband did not take reasonable compensation during the period the appreciation occurred or in which the corporation itself was a sham and fraudulent as to his wife. See the discussion of *Schorer v. Schorer*, 177 Wis. 2d 387, 501 N.W.2d 916 (Ct. App. 1993), in section 3.46, *supra*.

#### **4. Residential Real Estate [§ 3.48]**

The issues presented regarding the residential real estate of the parties differ from other cases involving mixing because often both labor is expended in connection with the upkeep or improvement of the property and capital items for the home, such as carpeting or a furnace, are purchased using funds of a different classification than the residence. The issue regarding labor mixing is whether the labor expended is sufficient to satisfy the standards of section 766.63(2) and thereby cause the appreciation in the value of the property during the marriage to be classified as marital property. The issue regarding marital property funds expended for improvements to a nonmarital property residence is the classification of the improvement and the consequences thereof.

*Lloyd*, 170 Wis. 2d 240, addressed the labor issue. Before the marriage took place, the husband acquired ownership of a residence, in

which the spouses lived during most of their marriage. The court of appeals held that although the circuit court had made no explicit finding regarding donative intent, it was clear from the testimony that the spouses meant to keep their respective property separate. The court of appeals then looked to the labor expended to maintain the property. The circuit court had found that the wife had used her funds to pay for the couple's food, clothing, and shelter expenses. The court of appeals held that this finding did not satisfy the legal standard set out in section 766.63(2). "The finding does not establish that the applied efforts of either spouse were anything more than performance of usual and normal marital responsibilities." *Id.* at 262. The court did not separately consider the use of marital property funds to maintain the residence. The court also held that there was no evidence of substantial, or even any, appreciation to the property. Thus, the court concluded that no portion of the residence was marital property.

In *Kobylski v. Hellstern (In re Estate of Kobylski)*, 178 Wis. 2d 158, 503 N.W.2d 369 (1993), the court addressed the expenditure of both labor and funds. Before marriage, the wife acquired ownership of a residence, in which both spouses lived during the marriage. During the marriage all of the funds received by the husband and the wife were deposited into joint accounts. The funds in those accounts were used to pay property taxes, utilities, insurance, and other related residence expenses. Also, the parties expended approximately \$4,000 from the joint accounts during the marriage for improvements to the residence, including new siding and gutters, carpet, a garage door, and building materials and concrete for a new garage. The husband testified that during the marriage he painted the interior and exterior of the residence, assisted in enlarging the garage, and did the yardwork around the residence. He testified that he received no compensation from the wife for these efforts.

The wife died, and the husband asserted a marital property interest in the residence. From these facts, the probate court concluded that the contribution of labor and the funds from the joint accounts for maintenance and improvements constituted a mixing of marital property with property other than marital property under section 766.63(1) and concluded that "because 'substantive labor, efforts and marital cash were applied' during the marriage and 'tracing is [not] possible as unreimbursed labor is involved,'" the entire residence was reclassified to marital property. *Id.* at 170.

The court of appeals first held that the burden of establishing the occurrence of mixing under section 766.63(1) was properly assigned to the party claiming a reclassification. Once that burden is satisfied, the party seeking to avoid reclassification has the burden of proof to trace the nonmarital property component. The court followed its decision in *Lloyd* in requiring the estate to establish that the identity of the property has been preserved. In performing the identity analysis, the issue is whether the nonmarital component has been preserved in an identifiable form so that it can be meaningfully valued and assigned. The court referred to the character analysis in *Lloyd* and held it did not apply to mixing issues under section 766.63. *Id.* at 173–74 n.7. The court clarified that character involves donative intent and that a character/gift/donative intent analysis under the Act is properly made using the reclassification by gift rules of section 766.31(10).

The use of marital property funds in the joint account to pay for improvements to the residence satisfied the burden of proof that the property was mixed under section 766.63(1). Thus, the question became whether the component of the mixed property that was not marital property could be traced. The court held that the estate satisfied its burden by the husband's proof of the amount of the contribution of marital property funds to the nonmarital residence. This gave a basis to segregate the nonmarital component.

The court of appeals then considered the appropriate remedy. It found that all community property states use both the ownership and reimbursement approaches. The court noted that the book stated that there was a preference in the Act for creation of an ownership interest. The court stated that decisions in a majority of community property states provide that improvements take on the classification of the property itself and also create a right of reimbursement. Determining that reimbursement was the correct approach in this case, the court held that the amount of the reimbursement should be the enhancement in the value of the property as a result of the improvements. It should not be the amount of marital property funds actually expended.

Thus, expenditures that relate merely to the maintenance of the property or which do not enhance the property's value are not to be considered. The party seeking such reimbursement has the burden of demonstrating that the improvement funds expended have enhanced the value of the spouse's separate property and the amount of enhancement.



*Id.* at 180; *see also Krueger v. Rodenberg*, 190 Wis. 2d 367, 527 N.W.2d 381 (1994). This analysis of ownership versus reimbursement approaches is an important step in Wisconsin law involving improvements to property.

The court of appeals then considered the labor-mixing issues. The probate court had held that the efforts constituted substantial uncompensated labor, serving to reclassify the entire residence to marital property. Regarding substantial appreciation, the probate court analyzed the assessed value of the property and its sale price. The probate court recognized that the property declined in value between the determination date and the date of death, but found that the labor expended contributed to the utility and comfort of the home. The probate court found the decline in market value was something not contemplated by the statute, a market value drop not related to the activity of the nonowning spouse while “substantive labor, efforts and marital cash were applied.” *Estate of Kobylski*, 178 Wis. 2d at 167.

The court of appeals reversed this portion of the probate court decision and held that under section 766.63(2), the claimant had to establish the contribution of his labor, that no reasonable compensation was received, and that the labor produced a substantial appreciation in the nonmarital asset. The court held that most of the husband’s efforts did not constitute the substantial efforts required by section 766.63(2). The court considered the UMPA explanation of substantial effort. It concluded that painting and yardwork, without more, qualify only as routine, normal, and usual property maintenance. The court did, however, find that the husband’s efforts in enlarging the garage qualified as a substantial contribution of industry and in a footnote stated it would not give an opinion on whether the appraiser’s testimony that a garage would increase the value of the residence by \$2,000 to \$3,000 would constitute evidence of substantial appreciation. *Id.* at 186–87 n.14. The probate court, however, had found no evidence of an increase in market value of the property as a result of the efforts and, fair or not, held that the legislature has decreed the contributing party may not recover for uncompensated substantial industry if there is no resulting substantial appreciation. *See also Bille*, 198 Wis. 2d 867.

The circumstances in *In re Marriage of Pearson-Maines*, 855 P.2d 1210 (Wash. Ct. App. 1993), were that before the marriage, the wife owned a residence that was used by the parties after the marriage. The residence was destroyed by fire during the marriage, and the wife

received an insurance settlement. The settlement proceeds as well as the parties' labor were used to rebuild the property. At the time of the divorce, the residence was worth \$50,000. Of that amount, \$28,000 was the amount expended from the settlement and the remaining \$22,000 stemmed from community effort. (The analysis does not include all the findings required by section 766.63(2).) The husband was entitled to reimbursement for the increased value of the property resulting from his efforts. However, the wife was entitled to compensation for the community benefit obtained from their occupancy of the property during the marriage. The rental value was \$11,000 for the period, reducing the community interest to \$11,000.

### **I. Passive Income from Labor [§ 3.49]**

Before the enactment of the 1985 Trailer Bill, labor applied to individual property during marriage did not create marital property unless the requirements of section 766.63(2) were satisfied. Section 766.63(2) dealt with appreciation in the principal value of the asset, and under the original Act all income from property of any classification was marital property. The 1985 Trailer Bill changed the rule on income from property other than marital property if a unilateral statement was filed. Wis. Stat. § 766.59. If a spouse has executed a unilateral statement, all income on assets other than marital property is individual property. This includes income on all predetermination date property and individual property.

If one spouse performs services that assist in the collection of income or that increase the amount of income earned that is otherwise classified as individual property because of a unilateral statement, is a portion of that income considered earned income and thus marital property? For example, if a parcel of individual, rental real estate is covered by a unilateral statement, and one spouse performs routine maintenance on the property, such as painting, plumbing and other repairs, and assists in the collection of the rental income, is a portion of that rental income deemed earned income and thus not covered by the unilateral statement? Such services would not satisfy the requirements of section 766.63(2). Moreover, if a portion of the rental income is considered earned income, the deposit of the rent check into an account with other individual or predetermination date property would invoke the mixing rule of section 766.63(1), thereby potentially reclassifying the entire income and assets acquired therewith to marital property. Because the portion that was

earned income would be difficult to ascertain on a periodic basis as the rent was received, it would be almost impossible to segregate the income into the appropriate components except by means of a marital property agreement. See McClanahan, *supra* § 3.12, at § 6:18.

Because classifying a portion of the income as earned income would entirely frustrate the intended benefits of a unilateral statement as authorized by the Act, no portion of the income covered by the unilateral statement should be considered marital property unless the services provided have some significance. In addition, to maintain the maximum effectiveness of the unilateral statement, it is appropriate to provide the marital estate with only a right to reimbursement for the value of the services, rather than creating an ownership interest that could also affect other assets and income. See Acres, *Community and Separate Property Characterization of Closely Held Business Interest in Texas*, 14 Community Prop. J., Oct. 1987, at 9; Perkins, *Appreciation of the Separately Owned, Closely Held Business*, 14 Cmty. Prop. J., Oct. 1987, at 62.

If, however, a portion of the income is deemed earned income, other community property jurisdictions have in analogous situations used two approaches to establish the respective shares. One theory is set forth in *Pereira v. Pereira*, 103 P. 488 (Cal. 1909). In that case, the court assumed that the separate property had produced income at a reasonable rate of return, and the court allocated that income to separate property. Under this approach, any balance in the income is community property. The second approach is set forth in *Van Camp v. Van Camp*, 199 P. 885 (Cal. Ct. App. 1921). In that case, the court determined a reasonable wage or salary for the services rendered. That amount was allocated as community property, and the balance of the income realized was separate property. For a discussion of the differences in applying the *Pereira* and *Van Camp* approaches, see *Cord v. Neuhoﬀ*, 573 P.2d 1170 (Nev. 1978). The appropriate approach in Wisconsin will depend on the facts and circumstances of each particular situation.



## Management and Control of Property During Marriage

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## **I. General Rules [§ 4.1]**

### **A. Scope [§ 4.2]**

This chapter discusses the rights of each spouse under the Wisconsin Marital Property Act, 1983 Wis. Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or Wisconsin Marital Property Act], to manage and control assets during marriage, including the authority to incur liabilities with respect to marital property assets and to commence and defend litigation over such assets. Management and control of marital property assets for the purpose of contracting for an extension of credit is discussed in chapter 5, *infra*. Marital property agreements, which can be used to modify the management and control rules, are discussed in chapter 7, *infra*.<sup>1</sup>

### **B. Management of Marital Property [§ 4.3]**

#### **1. In General [§ 4.4]**

Management and control is defined as “the right to buy, sell, use, transfer, exchange, abandon, lease, consume, expend, assign, create a security interest in, mortgage, encumber, dispose of, institute or defend a

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189; all references to the United States Code (U.S.C.) and Internal Revenue Code (I.R.C.) are current through Public Law Number 111-166 (excluding Pub. L. Nos. 111-148, -152, and -159) (May 17, 2010); and all references to the Code of Federal Regulations (C.F.R.) are current through 75 Fed. Reg. 28,739 (May 21, 2010). Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”



civil action regarding or otherwise deal with property as if it were property of an unmarried person.” Wis. Stat. § 766.01(11). All management and control rules may be varied by marital property agreement. *See* Wis. Stat. § 766.58(3)(b). The right to manage and control an asset—whether exclusive, in the alternative, or joint—does not determine the asset’s classification and does not rebut the presumption under section 766.31(2) that all property of spouses is marital property. Wis. Stat. § 766.51(5). The rights of management and control of an asset may be used to change the classification of an asset. Wis. Stat. § 766.31(10). This occurs if there is a gift to a spouse. *See infra* § 4.43.

➤ **Note.** The rules regarding management and control set forth in this chapter are partially limited by chapter 767 after the commencement of certain actions affecting the family, including divorce. Wis. Stat. § 767.117(1)(b). Without the consent of the other party or an order from the court, the parties to the action are prohibited from encumbering, concealing, damaging, destroying, transferring, or otherwise disposing of property owned by either or both of the parties except in the usual course of business, to secure necessities, or to pay the costs of the action. *Id.* Thus, investment decisions regarding assets or the incurring of debt to make an investment would require this additional approval without regard to the management and control rules in chapter 766. These statutes do not prevent changes in beneficiary designations for existing assets.

## **2. Determination of Whether a Marital Property Asset Is “Held” [§ 4.5]**

In determining spouses’ management and control rights for a specific marital property asset, the initial question is whether the asset is held in the name of one or both spouses. If the marital property asset is held in one spouse’s name, that spouse has exclusive management rights over the asset. Wis. Stat. § 766.51(1)(am). The comment to section 1 of the Uniform Marital Property Act (UMPA) (1983), *reprinted infra* app. A, indicates that the concept of holding was used instead of title because using the word “title” might have encouraged “overlooking the separate legal status of title and ownership, which is a fundamental aspect of the Act.”

Section 766.01(9) defines the term *held* as follows:

(a) Except as provided in pars. (b) to (d), property is “held” by a person only if a document of title to the property is registered, recorded or filed in a public office in the name of the person or a writing that customarily operates as a document of title to the type of property is issued for the property in the person’s name.

(b) An account is “held” by the person who, by the terms of the account, has a present right, subject to request, to payment from the account other than as an agent. Accounts that are so “held” include accounts under s. 705.01(1) and brokerage accounts.

(c) An uncertificated security, as defined under s. 408.102(1)(r), is “held” by the person identified as the registered owner of the security upon books maintained for that purpose by or on behalf of the issuer. If the registered owner of an uncertificated security is identified as a brokerage account, the security is “held” as provided under par. (b).

(d) The property rights, as specified and described in ss. 178.21 and 178.22, of a partner in a general partnership are “held” by the partner.

Under section 766.01(9), marital property real estate, for example, is held by one spouse if the deed to the real estate names that spouse as the grantee, because a deed is a writing that customarily operates as a document of title to real estate. The deed may but need not be “registered, recorded or filed” to confer exclusive management rights. *See Wis. Stat. § 766.01(9)(a)*. However, the management and control rights are limited if the real estate is homestead property. *See Wis. Stat. § 706.02(1)(f)*.

Like a deed to real estate, title to a marital property vehicle or boat confers exclusive management rights on the spouse named on the title. The title may but need not be registered in Wisconsin for the marital property asset to be considered held. *See Wis. Stat. § 766.01(9)(a)*.

A stock or bond certificate registered in one spouse’s name is a document that customarily operates as a document of title for a security, and such marital property security is held by the named spouse. A bill of lading, dock warrant, dock receipt, warehouse receipt, or order for delivery of goods in the name of one spouse is a document that customarily operates as a document of title and that causes the marital property asset to be held by the named spouse. *See Wis. Stat. § 401.201(15)*. A savings account passbook or certificate of deposit at a financial institution in one spouse’s name means that the marital property

account is held by that spouse. Checks representing marital property funds payable to a spouse are also held by that spouse.

However, some other written instruments regarding marital property assets are not likely to cause the asset to be held by a spouse or spouses. For example, it is unlikely that a bill of sale for household furniture or a deed of gift would cause the marital property asset described in those documents to be held by the named spouse. Although both documents may effectively transfer ownership, neither customarily operates as a document of title. Household furnishings may when sold be accompanied by a bill of sale, but their ownership could also be transferred by mere change of possession.

If no document of title exists, an asset is held if it meets the requirements of subsection 766.01(9)(b), (c) or (d). Under section 766.01(9)(b), an account is “held” by the person who, by the terms of the account, has a present right, subject to request, to payment from the account other than as an agent. Wis. Stat. § 766.01(9)(b). Section 766.01(9)(b) expressly includes bank accounts under section 705.01(1) and brokerage accounts. Thus, if one spouse opens an account with a brokerage firm, and the marital property securities are placed in the account and are registered in the nominee name of the brokerage firm, only the spouse who opened the account may direct transactions involving the securities.

➤ **Note.** Checking and investment accounts entail relationships based on a contract between a spouse or spouses and a third party. Contracts with a financial institution regarding a checking or investment account set forth who has access to the account and who may exercise further management rights regarding the assets in the account. If only one spouse is a party to the contract, then because of the express provision of section 766.01(9)(b), the other spouse does not have a right to change the terms of the contract with the third party but is instead limited to the remedies provided in section 766.70. *See infra* ch. 8; *see also infra* ch. 5 (regarding either spouse’s use of marital property assets to obtain credit).

Under section 766.01(9)(c), an uncertificated security is deemed to be held by the person identified as the registered owner on books maintained for that purpose. Under section 766.01(9)(d), the property rights of a general partner in a partnership are as described in sections

178.21 and 178.22. General partnership interests are deemed to be held by the general partner.

In addition to having the right to manage and control a marital property asset held in his or her own name, each spouse acting alone may also manage marital property assets *not* held in the name of *either* spouse. Wis. Stat. § 766.51(1)(am). Both spouses have the right to manage such property independently, and management is effectively determined by possession. Property that is not normally held in either spouse's name includes bearer securities, crops, jewelry, collectibles, artwork, animals, commodities (such as gold), cash, and furniture.

A marital property asset may be held in one spouse's name or may not be held in either spouse's name; in addition, marital property may be held in the names of both spouses. *See* Wis. Stat. § 766.60. If the spouses' names on a marital property asset are in the alternative (i.e., "H or W"), either spouse acting alone may manage and control the asset. Wis. Stat. § 766.51(1)(b). If any other form of holding that names both spouses is used, both spouses must act together to manage the asset (i.e., "H and W"). Wis. Stat. § 766.51(2).

The distinction between assets that are held by a spouse and assets that are not held by a spouse should not affect third parties dealing with married individuals. In either situation, if the asset is classified as marital property, the third party may become a bona fide purchaser. A third party bona fide purchaser may obtain status under the Act, the Uniform Commercial Code, or common law rules. *See* Wis. Stat. §§ 402.403, 766.57. The spouse who holds or, if the marital property asset is not held, has possession of the asset has the right to manage and control that marital property asset. The most important management power is the ability to contract with regard to the asset. This, among other powers, permits the purchase, sale, and encumbrance of the asset.

### **3. Management and Control of Joint-venture Interests and Other Contractual Assets [§ 4.6]**

The concept of assets being held, as developed in UMPA, is administratively functional for titled assets. The concept is difficult to apply to contract rights, which can represent assets of significant value. The only contract rights whose management is clearly determined are those expressly dealt with by statute. For example, contract rights in

brokerage accounts, bank accounts, and general partnerships are defined as held in the Act through special provisions not found in UMPA. *See* Wis. Stat. § 766.01(9)(b), (d).

General partnership interests are deemed to be held by the general partner under the definition of *held* in section 766.01(9). Wis. Stat. § 766.01(9)(d). However, the definition does not include limited partnership interests for which a certificate is not issued nor does it apply to other contractual assets. A joint-venture interest or limited partnership interest may be classified as marital property if this result is supported by an analysis of the classification of the capital contribution or funds used for the purchase. *See supra* § 2.51. However, a written joint-venture agreement or limited partnership agreement does not appear to be “a writing that customarily operates as a document of title to the type of property [which] is issued for the property in the person’s name.” Wis. Stat. § 766.01(9)(a). The agreement is not issued in a person’s name.

The Act as originally adopted did not include section 766.01(9)(b). 1985 Wisconsin Act 37 [hereinafter 1985 Trailer Bill] added the provision because accounts “appear not to be included in the general definition of property ‘held’ by a person.” Wis. Stat. Ann. § 766.01 Legis. Council Notes–1985 Act 37, §§ 69 to 73 (West 2009). If accounts were not held under the original Act, it does not appear that other contractual relationships could be considered held either. Joint venture contracts and limited partnership contracts have value and create rights and obligations but are not within the definition of held.

➤ **Query.** The general rule is that when an asset is not held, it may be managed by either spouse acting alone. Does this mean that a spouse who is not a party to the joint-venture agreement, limited partnership agreement, or other contract (the interest in which is classified as marital property) can transfer the joint-venture interest or contractual rights to a third party or exercise the contractual rights the same as a contracting party? If one spouse creates an individual retirement account (IRA) using marital property funds, may the noncontracting spouse change the beneficiary or exercise other rights? The answer is probably no. Before a joint-venture agreement, limited partnership agreement, or other contract is made, the contracting spouse must have the right to manage the marital property assets subsequently used for the capital contribution. The spouse may also contract for his or her services. Thus, when those assets or services are committed to a contract, the management rights should

not be altered or lost. After an agreement is made, only the parties to it should be able to exercise rights under the agreement.

#### **4. Special Rules: Life Insurance and Deferred-employment-benefit Plans [§ 4.7]**

The Act provides special management and control rules for certain types of marital property assets. Management rights to these assets are conferred without regard to whether the asset is all or partly marital property. Two assets with special management and control provisions are life insurance and deferred-employment-benefit plans. With regard to life insurance, the Act provides that a spouse acting alone may manage and control a life insurance policy if the spouse is designated as the “owner” on the policy issuer’s records. Wis. Stat. § 766.51(1)(d). Ownership set forth on a policy issuer’s records may differ from marital property ownership pursuant to the Act. *See* Wis. Stat. § 766.61(1)(a). For example, if a husband purchases a life insurance policy insuring his life before marriage, he will be listed as the owner on the records of the policy issuer and under the Act will have exclusive management and control rights. This power continues even though after the marriage he uses marital property funds to pay a premium, which creates a marital property ownership interest in the policy for his wife. For group life insurance, the term *owner* means the holder of each individual certificate of coverage under the group plan, regardless of whether the person is listed as the owner on the contract. *Id.*

➤ **Note.** Before 1987 Wisconsin Act 393 [hereinafter 1988 Trailer Bill], a written consent to a beneficiary designation or a consent as to the use of property to pay premiums was only possible for policies insuring the life of a spouse. Thus, the consent was not available for policies purchased to fund a cross purchase buy-sell agreement. *See infra* § 4.84. The 1988 Trailer Bill deleted the limitation. Under current law, written consents may be used on a life insurance policy insuring the life of any individual and providing for payment of death benefits at the insured’s death. Wis. Stat. § 766.61(1)(c). This revision is not in UMPA.

With regard to a deferred-employment-benefit plan, the Act provides that an employee spouse acting alone may manage and control his or her rights under the plan accruing as a result of that spouse’s employment.

Wis. Stat. § 766.51(1)(e). The employee has exclusive management even though the deferred-employment-benefit plan is all or partly marital property. For example, the employee spouse may select his or her retirement date, settlement options, and times of payment and also designate the beneficiary of such payments. *See* I.R.C. §§ 401(a)(9), (14), 417.

Neither of these special management provisions affects the classification of the asset or the remedies available to the other spouse. Wis. Stat. §§ 766.51(5), .70.

### **C. Management of Individual Property and Predetermination Date Property: General Rule [§ 4.8]**

Each spouse acting alone may manage and control his or her property that is not marital property—in other words, individual property and predetermination date property. Wis. Stat. § 766.51(1)(a). The Act grants the owner spouse the sole right to manage and control that spouse's property which is not marital property. *See id.* Section 766.51(6) expressly provides that the Act does not affect the right to manage either or both spouses' property acquired before the determination date. Thus, the right to manage and control predetermination date property is not affected by the Act and is the same right that existed under pre-Act law. However, unless a unilateral statement or marital property agreement is in effect, the income on the individual or predetermination date property is marital property, Wis. Stat. § 766.31(4), and if the marital property income becomes mixed with a nonmarital property asset, the nonmarital property asset may be reclassified as marital property. *See* Wis. Stat. § 766.63(1). If the nonmarital property component can be traced, different management and control rules may apply to the respective components. The income, which is marital property, is subject to marital property management and control rules.

### **D. Limits on Management of Marital Property [§ 4.9]**

The Act confers broad management rights on the spouse holding or possessing a marital property asset. Unlike the other community

property states, Wisconsin has no requirement of joinder in management actions, except with respect to actions involving the homestead or any marital property asset held in both spouses' names (other than in the alternative form). *See infra* §§ 4.44–.48. Nevertheless, the management powers are not unlimited.

The first limitation on management powers is the good-faith obligation. Each spouse has an obligation to act in good faith with respect to the other spouse in matters involving marital property assets or the other spouse's property. Wis. Stat. § 766.15(1); *see also infra* §§ 4.26–.33. The obligation of good faith, which is a lower standard than a fiduciary obligation, may not be altered by a marital property agreement. Wis. Stat. § 766.15(1); *see* UMPA § 2 cmt. The good-faith obligation does not apply to a spouse exercising management powers over his or her individual or predetermination date property. Wis. Stat. § 766.15(2).

The second limitation on management and control relates to a remedy available if one spouse acting alone makes substantial gifts of marital property assets to a third person. Under the Act, a spouse acting alone may give marital property assets in any amount to a third person. Wis. Stat. § 766.51(4). However, if the gift of marital property assets to a third person has an aggregate value exceeding (1) \$1,000 in a calendar year or (2) a larger amount if, when made, the larger gift is not reasonable in amount considering the spouses' economic position, the nondonor spouse has a remedy against the donor spouse, the donee, or both unless the spouses act together in making a gift. Wis. Stat. §§ 766.53, .70(6)(b); *see also infra* §§ 4.35–.42.

The Act's limitations protect the nondonor spouse's ownership interests. UMPA §§ 2, 6 cmts. Gifts defeat the nondonor spouse's interest in the donated property and thus make an absolute dollar limit appropriate, without regard to whether the donor spouse was acting in good faith. The general rule in other community property states applies a good-faith obligation to gifts of community property made by one spouse acting alone. William A. Reppy & Cynthia A. Samuel, *Community Property in the United States* 233–41 (2d ed. 1982). In one case in which the donor spouse could not remember how much money he gave away or to whom he gave it, the transfers were presumed fraudulent toward the nondonor spouse. *See Reaney v. Reaney*, 505 S.W.2d 338 (Tex. Civ. App. 1974). Similarly, another spouse was required to account for community property funds spent for gifts and favors connected with an



extramarital affair. *Simpson v. Simpson*, 679 S.W.2d 39 (Tex. App. 1984); *see also Carnes v. Meador*, 533 S.W.2d 365 (Tex. Civ. App. 1975). In Wisconsin, it appears that in a proper case, gifts of marital property assets made by one spouse acting alone may be challenged as violating the good-faith obligation even if the amount given to a third party is less than the amount permitted by section 766.53. *See infra* §§ 4.35–.42.

## **II. Substantive Differences from UMPA [§ 4.10]**

### **A. In General [§ 4.11]**

Since the Act is based on UMPA, it is appropriate in resolving questions under the Act to consider UMPA and its comments when the provisions are the same in both acts in resolving questions under the Act. Conversely, when the Act and UMPA differ, the Wisconsin legislative history should be examined to see why the UMPA provision was not used and the substantive impact of such differences. In addition to its special management and control provisions that apply in connection with incurring an obligation for the extension of credit (discussed in chapter 5, *infra*), the Act contains four provisions affecting management and control that differ from UMPA, discussed in sections 4.12–.15, *infra*.

### **B. Homestead [§ 4.12]**

UMPA provides for creation of “survivorship marital property” but, unlike the Act, does not provide that a homestead acquired exclusively by spouses is survivorship marital property, absent a contrary expression of intent in the instrument of transfer. UMPA § 11. (Under UMPA, a spouse may exercise management and control powers to create survivorship marital property if the term “survivorship marital property” is included in the document of title.) In the Act, a homestead acquired exclusively by spouses is survivorship marital property unless a contrary intent is expressed. The intent not to hold a homestead as survivorship marital property may also be expressed in a marital property agreement. *See* Wis. Stat. § 766.605. Thus, after the determination date, absent an intent to the contrary, a deed for a homestead to “A and B, husband and wife” or to “A and B” (if they are in fact married) creates survivorship marital property. *Id.* (Section 700.19(2), providing that such designation of spouses in a deed creates a joint tenancy, was amended by the Act to

apply only to property acquired before January 1, 1986 or while the Act does not apply.) A homestead may be reclassified in any manner provided in section 766.31(10). *Id.*

The decision in *Jones v. Estate of Jones*, 2002 WI 61, 253 Wis. 2d 158, 646 N.W.2d 280, dealt with a homestead property. The spouses had entered into a premarital agreement that provided for each party to hold all his or her solely owned property, including real estate, free of all rights or claims by the other party. The couple lived in a house that the husband owned before marriage; however, when the parties had been married for about 20 years, the husband transferred the home to the wife by warranty deed. Later that same day, the wife conveyed the homestead to her husband's two children with a reserved life estate. The husband did not sign this second deed. After the husband's death, the issue was whether the failure to have both spouses sign the deed as required in section 706.02(1)(f) made the transfer a nullity. The Wisconsin Supreme Court held that a spouse can waive the homestead protections in a premarital agreement; thus, it was not necessary in this case for both spouses to sign the deed for the deed to be effective.

### C. Life Insurance [§ 4.13]

Under UMPA and the Act, the owner of a marital property life insurance policy, as reflected on the policy issuer's records, has all management and control power over the policy, including the power to designate the beneficiary. *See* Wis. Stat. § 766.61(1)(a); UMPA § 12(a)(1); *see also infra* § 8.13. Even if the insured is the owner on the policy issuer's records, the insured's spouse may nevertheless have a marital property interest in the policy and its proceeds. Before the insured's death, the nonowner spouse can relinquish (or reclassify) any marital property interest in the policy and its proceeds by consenting (in writing) to either the designation of another person as beneficiary or the reclassification of the marital property interest. Wis. Stat. § 766.61(3)(e). UMPA section 12(c)(5) provides only for relinquishment and not for reclassification by consent. UMPA also presumes the nonowner spouse's consent to relinquish any interest when the beneficiary is a parent or child of either spouse. The Act omits this presumption. *See* Wis. Stat. § 766.61(3)(e).

➤ **Note.** Before passage of the 1988 Trailer Bill, a written consent to a beneficiary designation or to the use of property to pay premiums

was only possible for policies insuring the life of a spouse. Thus, the consent was not available for policies purchased to fund a cross purchase buy-sell agreement, *see infra* § 4.84. The 1988 Trailer Bill deleted the limitation. Under current law, written consents may be used on a life insurance policy insuring the life of any individual and providing for payment of death benefits at the insured's death. Wis. Stat. § 766.61(1)(c). The revision is not in UMPA.

The Wisconsin Act and UMPA also differ in another way with regard to life insurance. In Wisconsin, if (1) a spouse owns a policy on the other spouse's life and the policy-owning spouse dies first, or (2) a spouse has a marital property interest in a policy in which the insured spouse is the owner on the policy issuer's records and the noninsured spouse dies first, then the surviving spouse has the option of purchasing the decedent's interest in the policy from the estate at the interest's fair market value at the date of death. Wis. Stat. § 766.70(7). UMPA does not provide this option. *See infra* § 12.68.

#### **D. Deferred Employment Benefits [§ 4.14]**

The Act provides that a nonemployee spouse's marital property interest in a deferred-employment-benefit plan terminates at death if he or she predeceases the employee spouse. Wis. Stat. §§ 766.31(3), .62(5). Section 13 of UMPA does not provide for such termination. Thus, under the Act, the employee spouse's ability to manage and control deferred-employment-benefit plans and fully direct the beneficial interest in such plans is not affected if the nonemployee spouse dies first.

#### **E. Marital Property Agreements [§ 4.15]**

The provisions of the Act and UMPA differ with respect to the requisites for a valid marital property agreement vis-à-vis management and control. *See infra* ch. 7.

### III. Scope of Management and Control [§ 4.16]

#### A. Compensation for Services [§ 4.17]

##### 1. Earned Income [§ 4.18]

Compensation for services performed by a spouse after the determination date is marital property, absent a marital property agreement or court order to the contrary. Wis. Stat. § 766.31(4). Although the nonemployee spouse owns an undivided one-half interest in compensation received by the employee spouse for services during the marriage, Wisconsin statutes and employer-employee contracts generally require that the entire wage be paid to the employee. Wis. Stat. § 109.03(1). Absent a court order, the other spouse is not entitled to direct receipt of such wages. *See infra* § 8.40; *see also* Wis. Stat. § 109.03(3) (regarding payment of compensation after death of employee). However, in most situations, the employee spouse needs the nonemployee spouse's written consent to make an assignment of wages. Wis. Stat. § 241.09. A nonemployee spouse's interest in compensation, as well as in other marital property assets, is further protected by the duty of good faith under section 766.15. *See infra* §§ 4.26–.33. It appears that a nonemployee spouse may also seek remedies provided under the Act to limit or terminate the employee spouse's management and control rights and change the classification of compensation to the individual property of the nonemployee spouse. *See* Wis. Stat. § 766.70(4)(a) 1., 2.; *see also infra* § 8.40. These remedies are discretionary with the court and are discussed in chapter 8, *infra*.

Compensation is usually paid by check, in cash, or by direct deposit. Management and control rights differ under each of these alternatives.

1. *Compensation paid by check.* If compensation is paid by check, the funds represented by the check (a writing that customarily operates as a document of title to this type of property) are held by the employee spouse and are subject to his or her exclusive management and control. Wis. Stat. §§ 766.01(9), .51(1)(am); *see also infra* § 8.40. This permits the employee spouse to solely manage the funds. The funds may be deposited into an account at a financial institution or may be used to purchase assets. The account or assets so acquired may be titled as the employee spouse directs, but they remain classified as marital property.

2. *Compensation paid in cash.* Compensation that is paid in cash is not property held by the employee spouse; thus, under the Act, either spouse acting alone has the right to manage the cash. Wis. Stat. § 766.51(1)(am). Actual management rights are determined by possession.
3. *Compensation paid by direct deposit.* If compensation is directly deposited into an account at a financial institution, the employee spouse selects the account into which the deposit is made and may, as a result, control subsequent management by how the account is titled.

In all events, the resulting management and control rights are subject to the obligation of good faith and the other spouse's remedies.

## **2. Deferred Employment Benefits [§ 4.19]**

### **a. General Rules and Federal Law [§ 4.20]**

*Deferred employment benefit plan* is a term defined under the Act, and it includes most employer retirement plans and deferred compensation. See Wis. Stat. § 766.01(4). To the extent benefits are attributable to employment occurring during marriage and after the determination date, they are marital property. (The nonemployee spouse's marital property interest in a deferred-employment-benefit plan, or in assets in an IRA that are traceable to the rollover of a deferred-employment-benefit plan, terminates if he or she predeceases the employee spouse. Wis. Stat. § 766.62(5). A marital property agreement that classifies a deferred employment benefit as marital property does not affect the operation of this terminable interest provision unless the marital property agreement expressly provides otherwise. Wis. Stat. § 766.58(7)(a)).

If the employment and accrual of benefits began before the determination date, the benefits are mixed property subject to the proration rules of section 766.62(2).

The right to manage and control deferred employment benefits resides exclusively in the employee spouse under section 766.51(1)(e). Thus, depending on the type of benefit plan, the employee spouse may have the right to designate a beneficiary, select payment options, select time for payments to begin, request loans from plan assets, request in-service

withdrawals, and request withdrawals upon termination of employment, subject to the federal limitations discussed below.

1993 Wisconsin Act 160, which expanded the scope of the terminable-interest rule to include the marital property portion of the assets in an IRA that are traceable to the rollover of a deferred employment benefit plan, did not similarly expand the scope of section 766.51(1)(e). Thus, the right to manage and control an IRA continues to be determined under the general rules of section 766.51.

Federal law regarding tax-qualified defined benefit plans under I.R.C. § 401 protects the nonemployee spouse by requiring a joint and survivor annuity or the actuarial equivalent. Profit-sharing plans can avoid the joint and survivor annuity only if the spouse is named as primary beneficiary. These beneficiary provisions may be changed only with the nonemployee spouse's written consent. I.R.C. §§ 401(a)(11), 417. Under the Act, if the employee designates a beneficiary other than his or her spouse, the surviving spouse may recover his or her marital property interest in the plan from the beneficiary. *See* Wis. Stat. § 766.70(6)(b).

➤ **Practice Tip.** If a federal consent is executed, there may be federal preemption of the Wisconsin rule for plans covered by the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. §§ 1001–1461. *See supra* §§ 2.214–.217. Until the uncertainty is resolved, if the spouses wish to provide that a beneficiary other than the spouse will receive more than one-half the proceeds, it may be advisable for the spouses to have a marital property agreement classifying the plan benefits as individual property to ensure the effectiveness of the beneficiary designation.

One planning technique to obtain maximum benefit of the applicable credit amount for federal estate tax purposes has been to classify the assets in a deferred-employment-benefit plan as marital property and override the terminable-interest rule. If this technique is adopted and the nonemployee spouse dies first, one-half of the plan's assets are part of the nonemployee spouse's estate and can be used to fund the applicable exclusion amount (formerly the "credit shelter gift").

➤ **Caution.** The U.S. Supreme Court has determined that ERISA preempts state law permitting a transfer such as that described in the preceding paragraph, and therefore the exercise of management and

control over ERISA plans is limited. *Boggs v. Boggs*, 520 U.S. 833 (1997).

**b. Limitations on Management and Control:  
Analogy to Community Property Divorce  
Cases [§ 4.21]**

Under the Act, the basic limitation on the exercise of management and control rights is the spousal obligation of good faith. Cases in other community property states and some common law property states regarding the exercise of certain management rights may provide guidance in Wisconsin as to the scope of the employee spouse's good-faith obligation in protecting the nonemployee spouse's interest. Some California divorce cases are illustrative.

➤ **Note.** In California, only community property is subject to division in a divorce proceeding. This places a premium on classifying assets as community property and may have affected the outcome in the cases discussed below.

In *Gillmore v. Gillmore*, 629 P.2d 1 (Cal. 1981), the court held that a husband could not unilaterally determine when his former wife would receive her interest in the pension benefits attributable to his employment during the marriage. At the time of divorce, the trial court had reserved jurisdiction over the husband's interest in a retirement plan. Shortly after the judgment of dissolution was final, the husband, who intended to work for several more years, became eligible for benefits under the company retirement plan. His former wife filed a petition to obtain her share of the pension benefits immediately.

The court found that the benefits had matured because the only condition on the husband's enjoyment of the benefits was his retirement—a condition within his sole control. The court held that the husband could not invoke a condition wholly within his control (continuing to work) to impair his former wife's interest in those retirement benefits and defeat her community property interest.

The court further held that the husband had the right to postpone receipt of his pension and to run the risk that he might die before that date, but he was not free to force his former wife to do so as well.

According to the court, one spouse's financial situation may involve factors significantly different from the other's. After divorce, each spouse should be able to make an independent decision about how to handle his or her share of the former community property. Under the court's analysis, the employee spouse retains the right to change or terminate employment, agree to a modification of the retirement benefits, and elect between alternative benefits. However, if the right to choose among alternative retirement benefits is exercised in a way that impairs the nonemployee spouse's interest, the nonemployee spouse must be compensated. *Cf. Brooks v. Brooks*, 767 S.W.2d 358 (Mo. Ct. App. 1989) (similarly holding that a husband could not retire early, thereby adversely affecting his spouse by reducing retirement benefits).

*Stenquist v. Stenquist*, 582 P.2d 96 (Cal. 1978), concerned a further limitation on a spouse's right to elect a particular pension. The husband, a former member of the armed forces, had an opportunity at retirement to choose between a disability pension that would provide 75% of his basic pay and a retirement pension that would provide 65% of his basic pay. Under California law at the time and federal preemption rules, a disability pension was the husband's separate property, whereas a retirement pension was community property. In 1970, the husband, while still married, retired and elected the disability pension. In 1974, the husband commenced an action for divorce and claimed the disability pension as his separate property.

The court held that the employee spouse had the management right to select which pension benefit would be received but also held that if the employee elected the disability pension, the benefit would be apportioned between the spouses so that the retirement pension amount (65% of basic pay) would be considered a community asset divisible at divorce.

➤ **Note.** In Wisconsin, a disability pension may have components with different classifications. Part of the disability pension could compensate for loss of income during marriage (marital property), while another part could represent a recovery for personal injury or loss of income after marriage (individual property). *See supra* § 2.136. If so, the computations and resulting management rights in *Stenquist* could apply in Wisconsin.

Another pension case, *Lucero v. Lucero*, 173 Cal. Rptr. 680 (Ct. App. 1981), concerned a former spouse's right to participate in a redeposit



after separation (the end of the creation of community property rights) and thereby share in the resulting increase in pension benefits. The husband worked for the federal government from 1942 until his retirement in 1977, receiving credit for more than 30 years of employment service. In 1966, while married, he had withdrawn his retirement contributions and expended them for community purposes. To obtain the maximum retirement benefit, he had to redeposit \$9,373, which redeposit would increase the monthly pension by \$366 plus subsequent cost-of-living increases. In 1977, after the spouses' separation, the husband redeposited this amount, using his separate funds. The wife claimed that she was entitled to participate in the increased pension resulting from the redeposit as if she had paid a pro rata share of the redeposit. The court agreed.

The court held that the duty of spouses to deal fairly with each other does not terminate when they separate and dissolve their marriage. One spouse cannot, by exercising a management right wholly within his or her control, defeat the community interest. The court held that to allow the husband the sole right to decide whether to redeposit and the sole right to elect whether to redeposit with separate or community funds would be to treat the redeposit right as the husband's separate property. According to the court, the redeposit right was a pension right. The community owned all pension rights attributable to employment during the marriage, and the court thus permitted the wife to contribute to the redeposit and obtain a portion of the additional annuity as if it had been purchased with community property.

### **c. Conclusion [§ 4.22]**

The Act grants the employee spouse the right, acting alone, to manage and control a deferred-employment-benefit plan that accrues as a result of that spouse's employment. Wis. Stat. § 766.51(1)(e). However, ERISA restricts the employee spouse's ability acting alone to make third parties the beneficiary of certain plan benefits (or permits the nonemployee spouse to exercise certain options). In addition, as the cases in section 4.21, *supra*, illustrate, a court is likely to compensate the nonemployee spouse (or permit the nonemployee spouse to exercise certain options) when the employee spouse's management decisions adversely affect the nonemployee spouse's economic interests. In Wisconsin, the good-faith obligation can be applied to limit the exercise

of the right to manage and control deferred-employment-benefit plans during marriage.

### **3. Group and Split-dollar Life Insurance [§ 4.23]**

A group life insurance policy arising from employment commencing after the determination date is classified entirely as marital property. Wis. Stat. § 766.61(3)(a)1. A time-apportionment formula will apply to the policy if, after its issuance, either or both of the spouses are at any time not domiciled in Wisconsin. Wis. Stat. § 766.61(3)(a)2. If the policy was issued before the determination date, it has a marital property component. Wis. Stat. § 766.61(3)(b). In determining the marital property component of the ownership interest and proceeds of a group policy sponsored by an employer or association, the date on which the policy becomes effective is the date on which the individual coverage begins, notwithstanding that the employer or association thereafter changes policy issuers or that the amount of coverage changes under the policy pursuant to the plan or benefit offered by the employer or association. Wis. Stat. § 766.61(2m)(b). If additional underwriting is required after original issuance of the policy, the effective date of the policy is the date on which the newly underwritten coverage begins. *Id.* These rules may be changed by a marital property agreement or written consent. Wis. Stat. §§ 766.58(3), .61(3)(e).

If the noninsured spouse predeceases the insured spouse, the decedent's marital property interest in a policy that designates the surviving spouse as the owner (as defined, with regard to group insurance, in section 766.61(1)(a)) and insured is limited to a dollar amount equal to one-half of the marital property interest in the interpolated terminal reserve and in the unused portion of the term premium of the policy on the date of death of the deceased spouse. Wis. Stat. § 766.61(7). All other rights of the decedent spouse terminate upon death. *Id.* A marital property agreement may change this result only if it expressly provides for the different result. Wis. Stat. § 766.58(7)(b).

For purposes of management and control, group and split-dollar life insurance are not considered benefits under a deferred-employment-benefit plan, *see* Wis. Stat. § 766.01(4)(b); thus, the special management rules governing such plans, *see supra* §§ 4.19–.22, do not apply. The group and split-dollar life insurance policies do, however, fall within the exclusive management and control of the employee spouse, since the

employee spouse initially is designated as owner on the policy issuer's records. *See* Wis. Stat. § 766.51(1)(d). The management and control powers include the power to designate a beneficiary of the policy proceeds and to assign ownership of the policy.

If group or split-dollar life insurance is marital property, in whole or in part, and if a beneficiary other than the surviving spouse is designated to receive more than one-half of the marital property proceeds, then upon the death of the employee owner spouse the surviving spouse can recover his or her marital property interest from the beneficiary. *See Socha v. Socha*, 204 Wis. 2d 474, 555 N.W.2d 152 (Ct. App. 1996); *see also* Wis. Stat. § 766.70(6)(b); *infra* § 8.51. This remedy exists unless (1) the nonemployee spouse gives written consent to the designation of another person as beneficiary of the proceeds or to the use of marital property to pay premiums, or (2) the nonemployee spouse has executed a marital property agreement or a written consent reclassifying the policy. *See* Wis. Stat. § 766.61(3)(e). The consent may cover insurance coverage attributable to subsequent premium payments. *Id.*

➤ **Comment.** Even if the spouses so intend, it is unclear whether a written consent as to beneficiary designation or classification of a split-dollar policy is effective for additional coverage purchased with subsequent dividend additions classified as marital property. *See* Wis. Stat. § 766.01(10); *see also infra* ch. 10. The better view is that such policy dividends are property used to pay premiums, and thus the consent is effective.

The employee spouse who owns a group or split-dollar insurance policy may name a creditor as the policy beneficiary. In addition, the owner of a split-dollar policy may, unless prohibited by the split-dollar agreement, assign the policy to a creditor as collateral for an obligation. (Assignment to a creditor is not effective for group life policies. *See* Wis. Stat. § 632.56(3).) If a creditor is named as beneficiary or if an assignment occurs, the creditor's interest in the proceeds is superior to the other spouse's marital property interest to the extent of the consideration paid by the creditor. *See* Wis. Stat. § 766.61(4); *see also Bille v. Zuraff (In re Estate of Bille)*, 198 Wis. 2d 867, 543 N.W.2d 568 (1995). This provision giving creditors priority allows an employee spouse to use a beneficiary designation or assignment to preserve his or her individual property.

➤ *Example.* If an asset is acquired that creates an obligation in the interest of the marriage or the family and the only funds available to satisfy the obligation are individual property, the use of the individual property to satisfy the obligation may be presumed a gift. *See supra* § 3.40. When new funds are received through salary, they are classified as marital property and the individual property is depleted. A right of reimbursement exists only if there is an agreement between the spouses. *Id.* If the spouse instead obtains a loan using the marital property insurance policy as security, the loan proceeds can satisfy the obligation and preserve any individual property funds. The exercise of this management and control alternative is subject to the obligation of good faith. *See Wis. Stat. § 766.15(1).*

An employee spouse who owns an interest in a group or split-dollar life insurance policy has the additional management power to assign ownership of the interest by gift to a third party, which may include transferring the interest to an irrevocable life insurance trust. *See Wis. Stat. § 766.51(1)(d).* Such transfers are subject to the restrictions on gifts, the obligation of good faith, and the interspousal remedies. *See infra* §§ 4.26–.33, .35–.42, 8.46. A gift of a life insurance policy is valued for this purpose at the amount that would have been payable if the insured had died when the gift was made; this amount is used to determine whether the amount of the gift was reasonable. *Wis. Stat. § 766.53; see also infra* §§ 4.37, ch. 10.

#### 4. Stock Options [§ 4.24]

Stock options granted to an employee spouse for services performed after the determination date are compensation for services and thus are marital property. *See Wis. Stat. § 766.31(4).* It is unclear whether stock options issued under a corporate plan are within the definition of deferred-employment-benefit plans under section 766.01(4)(a). If the statute is interpreted so that stock options are a deferred-employment-benefit plan, the employee spouse has exclusive management of them. *See Wis. Stat. § 766.51(1)(e).* On the other hand, if the stock options are not a deferred-employment-benefit plan, the option-grant contract appears to determine the parties' rights and can subject the option to the employee spouse's exclusive management and control. *See supra* § 4.6.

## **5. Other Benefits [§ 4.25]**

Employee benefits take many forms. Some employers provide group health insurance and group disability insurance coverage. Others provide employees with paid vacations, use of automobiles, club memberships, and other benefits.

After the determination date, employee benefits are classified as marital property because they are economic benefits having value attributable to a spouse's efforts. *See* Wis. Stat. § 766.01(10). Such benefits do not qualify as a deferred-employment-benefit plan. One exception is when the right to payment accrues on a disability plan, *see* Wis. Stat. § 766.01(4)(b); the right to payment is converted to a benefit under a deferred-employment-benefit plan, and the employee spouse has exclusive management rights. *See supra* §§ 4.19–.22. Otherwise, employee benefits fall within the definition of wages and thus must be paid to the employee. *See* Wis. Stat. §§ 109.01(3), .03. At dissolution or death, benefits that have a monetary value may be divided. *Bloomer v. Bloomer*, 84 Wis. 2d 124, 267 N.W.2d 235 (1978); *Lorenz v. Lorenz*, 194 Cal. Rptr. 237 (Ct. App. 1983); *Hewett v. Hewett*, 160 Cal. Rptr. 1 (Ct. App. 1979) (ordered not published).

## **B. Good-faith Duty [§ 4.26]**

### **1. In General [§ 4.27]**

#### **a. Analysis of Wisconsin Statute [§ 4.28]**

In the exercise of management and control over marital property assets or the other spouse's property, all transactions are subject to review by the other spouse. The overriding obligation of both spouses is to act in good faith. Under section 766.15(1), “[e]ach spouse shall act in good faith with respect to the other spouse in matters involving marital property or other property of the other spouse.”

Section 766.15(1) is identical to UMPA section 2(a). Neither section explains the actual duty of good faith or gives examples of permitted or prohibited conduct. The comment to UMPA section 2 refers the reader to William A. Reppy, Jr., *Community Property in California* 174–75, 177 (1980), and to section 5125(e) of the California Civil Code.

California's statute, described as "similar" to UMPA section 2(a), became effective in 1975, when the state changed to an equal management system. The comment to UMPA section 2 explains that spouses are not trustees or guarantors toward each other, but that they are more than "simple parties to a contract endeavoring to further their individual interests." *See infra* § 8.12.

Several Wisconsin statutes require good faith in commercial situations. *See, e.g.*, Wis. Stat. §§ 401.201(19), .203, 402.103(1)(b), 421.108. Although findings regarding good faith have been made in a few cases involving those statutes, those cases do not analyze the requirements of the standard, and the decisions are of limited relevance to a spousal relationship. *See Crown Life Ins. Co. v. La Bonte*, 111 Wis.2d 26, 330 N.W.2d 201 (1983); *First Am. Nat'l Bank v. Fiesta Corp.*, 25 Bankr. 236 (Bankr. W.D. Wis. 1982).

Section 766.15(2), which immediately follows the good-faith obligation in subsection (1), provides that "[m]anagement and control by a spouse of that spouse's property that is not marital property in a manner that limits, diminishes or fails to produce income from that property does not violate sub. (1)." Thus, a spouse does not have a good-faith obligation to produce income with his or her individual or predetermination date property.

➤ **Comment.** A logical inference might be that while individual property and predetermination date property may be so managed, marital property assets may not be managed or controlled to intentionally limit, diminish, or fail to produce income. If correct, this reading would severely restrict permissible investments and prohibit investment in nonincome-producing assets, such as vacant real estate or securities that do not pay dividends. The comment to UMPA section 2(b) does not support this interpretation. The comment states that subsection (2) was included to resolve any questions that might arise regarding the application of subsection (1) to the income stream of property that is not marital property. Subsection (2) should be limited to this purpose and not be construed to create affirmative obligations regarding marital property assets.

The obligation of good faith was considered in *Lloyd v. Lloyd (In re Estate of Lloyd)*, 170 Wis.2d 240, 487 N.W.2d 647 (Ct. App. 1992). The husband established accounts in joint tenancy with a third party after a divorce proceeding was commenced and in violation of a court order.

The circuit court held that the accounts were fraudulent because they were established in violation of a court order. The court of appeals agreed and also stated: “We agree that all [of the accounts] are marital property because they were established after the determination date with funds not clearly shown to be nonmarital. Thus, the transfers also constituted a breach of the spousal duty of good faith.” *Id.* at 264; *see also Gardner v. Gardner*, 175 Wis. 2d 420, 499 N.W.2d 266 (Ct. App. 1993).

In *Socha*, 204 Wis. 2d 474, the parties commenced a divorce proceeding, and the court entered an order restraining both parties from disposing of marital property assets. The husband changed the beneficiary of his group life insurance and Wisconsin Retirement System death benefit from the wife to his son. The husband died before the divorce was concluded, and the wife commenced an action to recover the proceeds. The court held the change of beneficiary to be a breach of good faith.

### **b. Analogy to Other Community Property States** **[§ 4.29]**

The other community property states recognize a duty between spouses regarding the management of community property. Reppy & Samuel, *supra* § 4.9, at 245. Some decisions from these jurisdictions refer to this duty as a fiduciary duty. William Q. de Funiak & Michael J. Vaughn, *Principles of Community Property* §§ 113, 119, 120, 150 (2d ed. 1971). However, most of these cases were decided before those states changed from sole male management to equal management, and the analysis of the duty between spouses is different from that applied to a trustee. *See Williams v. Williams*, 14 Cal. App. 3d 560, 92 Cal. Rptr. 385 (1971); *see also infra* § 8.12.

The cases in other community property states illustrate the kind of fact situations from which allegations of lack of good faith may arise in Wisconsin. Those cases, especially those that have arisen in California after January 1, 1975, and were decided under a similar statute, should provide some guidance in determining the scope of the good-faith obligation in Wisconsin. Generally, the facts in those cases that support a finding that there was no breach of fiduciary duty would also support a finding that there is no breach of the good-faith obligation under section 766.15. However, if the court finds that there was a breach of fiduciary

duty—a higher standard than that imposed by section 766.15(1)—the facts involved may not support a finding that there has been a breach of the good-faith obligation under the Act.

## 2. Investments [§ 4.30]

To date there are no Wisconsin decisions regarding the good-faith obligation by a spouse in handling investments. The cases from other states show the type of issues that can arise. The spouse's obligation of good faith in connection with an investment opportunity was considered in *Ogden v. Ogden*, 331 So. 2d 592 (La. Ct. App. 1976). The husband had used community property to acquire stock in a closely held family corporation. After the spouses were legally separated but before their divorce, the corporation offered additional stock for sale under preemptive purchase rights attributable to the original stock. The husband used his separate funds to purchase the additional stock. The trial court held that the acquisition was community property because the preemptive rights were attributable to the original community property securities purchased before separation. The appellate court affirmed, stating that after separation the husband still had a fiduciary duty to his wife with regard to the management of community property. The appellate court held that when an investment opportunity arises from community property assets, it is a community opportunity of which the spouse must take advantage if community funds are available. The spouse may not change the classification of the purchase rights derived from the original community property stock by using separate funds. Moreover, if the spouse does not take advantage of the investment opportunity for the community, he or she must make full disclosure of the opportunity so the other spouse might exercise the preemptive right.

The issue of good faith in investment opportunities arising from employment of a spouse during marriage was considered in *Somps v. Somps*, 58 Cal. Rptr. 304 (Ct. App. 1967). The husband was a partner in a partnership commenced before marriage. The cash accumulated from his work in the partnership was allocated 60% separate property and 40% community property. The husband used his separate funds to purchase real estate with his partner and a third party; the property was later sold for a substantial profit. The investment opportunity was tangential to the husband's employment. The issue was whether the husband had breached his fiduciary relationship by using separate funds rather than available community funds to acquire the investment. The court held



that the husband did not breach his fiduciary duty, stating that there “is no reason why husband should be compelled to keep his separate funds idle.” *Id.* at 310. In so holding, the court noted that the husband had apparently made many investments that benefited the community.

The handling of an investment was also considered in *Baum v. Baum*, 584 P.2d 604 (Ariz. Ct. App. 1978). The husband received a gift from his father of numerous shares of a closely held corporation. The shareholders subsequently sold their shares to B.F. Goodrich Company. By separate agreement, the husband acquired from B.F. Goodrich an option to purchase those shares for a fixed price if the business relationship continued and the husband continued as manager. The husband transferred the option to the closely held corporation for no consideration. One year later, during the marriage, the corporation exercised the option and repurchased the stock. Of the purchase price, almost 90% was paid by the corporation from its retained earnings during the marriage.

In the divorce proceeding, the wife claimed that the option had a value that was a community asset. The court held that even if the option were a community asset when it was offered to the husband, its value certainly was not the same as the total purchase price of the stock, and the wife did not establish the option’s value. Moreover, the court held that regardless of the option’s value when it was offered to the husband, the community lost any rights to it when the husband transferred the unexercised option to the closely held corporation. The community had not paid anything for the option, nor did the records support the allegation that the husband acted improperly to benefit his separate property at the expense of the community. No evidence was presented establishing that the community was interested in exercising the option or that it was in a position to do so. Thus, the court held that the community did not retain rights in the option when it was transferred.

Although the obligation of good faith applies to investments, the cases in the other community property states do not state a consistent standard by which to test a spouse’s management decisions. In contrast to older cases, more recent cases are similar to *Somps* and *Baum* in refusing to second-guess management decisions. *Reppy & Samuel, supra* § 4.9, at 245–46.

➤ **Query.** What effect does the spouses’ separation have on the good-faith standard for testing a spouse’s management decisions?

The *Lucero* decision discussed at section 4.21, *supra*, and the *Ogden* decision discussed earlier in this section concern management and control after spouses separate. In Wisconsin, after spouses have separated, it is possible to obtain a judgment of legal separation under chapter 767 that constitutes a dissolution for purposes of the Act and thus affects management of assets that were classified as marital property. See Wis. Stat. § 766.01(7); see also *infra* § 11.29. If a judgment of legal separation is not obtained, is the measure of the good-faith obligation applicable after separation different from that applicable before separation? See *infra* § 4.57. The courts may, however, consider this fact in applying the obligation of good faith and in deciding cases under the equitable remedies provisions in section 766.70. See *infra* § 8.12.

The issue whether a spouse breached the duty of good faith with regard to an asset classified as marital property was raised in *Noble v. Noble*, 2005 WI App 227, 287 Wis. 2d 699, 706 N.W.2d 166. In that case, two brothers, Dale and Danny, were partners in a partnership that farmed numerous properties. The land farmed by the partnership was not owned by the partnership. The two brothers owned some of the land as tenants in common. During Danny's marriage, three different parcels of land that the partnership farmed became available for purchase, and the brothers decided that Dale and his wife should purchase the three parcels. The partnership financed the purchase and created a ledger showing the amount receivable from Dale.

In the divorce action, Danny's wife claimed that her husband breached the obligation of good faith by not purchasing a one-half interest in the three properties when they became available for purchase. She claimed that by not purchasing an interest in this real estate the husband committed marital waste. She requested as a remedy that the court include the value of the three properties in the divisible estate for purposes of the property division.

The court held that "once the divorce action is filed, the section 766.15 cause of action and its attendant remedy are no longer available." *Id.* ¶ 18. Once the divorce action was started, sections 767.255(3) and 767.275 (since renumbered as sections 767.61(3) and 767.385) became applicable. Under those statutes, it does not matter that the husband refused to purchase the properties in large part for the purpose of keeping them out of the divisible estate. The statutes are designed to prevent squandering or destruction of marital property or the unjustified

depletion of divisible assets. Neither statute “require[s] a party to a pending divorce to take advantage of an opportunity to acquire property that would *increase* the value of the marital estate. This is so even if the opportunity represents a good deal.” *Id.* ¶ 19. The fact that Danny permitted partnership funds to be used to finance the purchase of the real estate by Dale and his wife did not constitute waste, squandering, destruction, or unjustified depletion of marital assets.

### 3. Litigation [§ 4.31]

One power of management and control is the right to institute or defend a civil action regarding an asset classified as marital property. Wis. Stat. § 766.01(11). Once commenced, an action must be pursued in good faith with regard to the other spouse. The obligation of good faith in the conduct of litigation involving community assets and obligations was considered in *Schultz v. Schultz*, 164 Cal. Rptr. 653 (Ct. App. 1980). The court in the divorce action ordered the residence sold to satisfy certain creditors. One obligation was based on a community debt owed to a third party. The third party filed suit to collect the debt against the husband, who did not have counsel and apparently failed to appear on the trial date.

After the residence was sold, the trial court allocated the debt unequally because of the husband’s failure to defend the suit properly. The appellate court held that the circumstances in this case were not sufficient to permit unequal division. (California at that time only authorized unequal division if a spouse had deliberately misappropriated community property. *See* Cal. Civ. Code § 4800(b)(2) (West 1983).) The court held that *deliberately misappropriated* refers to calculated thievery as opposed to mishandling of assets, although the phrase could also apply to gross mishandling of community financial affairs tantamount to fraud.

In Wisconsin, a spouse who brings an action to enforce a claim involving a marital property asset or who is a defendant in an action in which the obligation may be satisfied from property classified as marital property should be aware of his or her good-faith obligation to properly represent the spouses’ interests. *See* Wis. Stat. § 766.15(1); *see also infra* §§ 4.49–.56. If, for instance, a spouse allows a default judgment to be entered in an action in which a defense exists, the spouse may breach the obligation of good faith. *See infra* § 8.12.

#### 4. Accounting for Marital Property [§ 4.32]

Section 766.70(2) authorizes a spouse, both during the ongoing marriage and at dissolution or death, to obtain an accounting of the spouses' property and obligations. *See* UMPA § 15 cmt. Most other community property states recognize the duty to account for management transactions and assets only at dissolution or death. Reppy & Samuel, *supra* § 4.9, at 249.

In the other community property states, the obligation of good faith requires a spouse in a dissolution to be able to account for community property in his or her possession. *Id.* at 247. By contrast, in Wisconsin the duty is separately stated, and a court may order a spouse during marriage to account for the spouses' property and obligations. *See* Wis. Stat. § 766.70(2). Thus, in Wisconsin a failure to account gives rise to the determinations in section 766.70(2). It is unclear whether in Wisconsin a failure to account would also violate the duty of good faith. Despite this ambiguity, the cases in other community property states should help determine the extent to which a spouse domiciled in Wisconsin must account for expenditures or disposition of marital property assets.

The good-faith obligation to account for community property in a spouse's possession was considered in *Valle v. Valle*, 126 Cal. Rptr. 38 (Ct. App. 1975). The parties were divorced, and the appeal involved the division of community property. The husband contended that two community property assets, a parcel of real property in Mexico and an automobile, should not have been allocated to him in the property division because he no longer held the property, which had been taken by creditors. The court held that the husband's uncorroborated testimony was not sufficient to prove that the disputed assets had been taken by third-party creditors in discharge of community debts. The husband was required to produce documentary evidence of the obligations, the transfer of the automobile title, and the foreclosure sale. The appellate court held that absent such evidence, the trial court had correctly allocated the assets to the husband because he was last in possession. The fact that the assets were lost after the spouses had separated does not appear to have affected the analysis.

The good-faith obligation to account for community funds was raised in *Reaney v. Reaney*, 505 S.W.2d 338 (Tex. App. 1974). In the divorce action, the husband testified that he had spent \$53,000, losing some

through gambling and giving some away to strangers. The court held that the husband, who had the burden of proof, had failed to show that the loss and dissipation of the community funds were not an abuse of his managerial powers. Consequently, the court entered a damage judgment against him in favor of the wife.

In the other community property jurisdictions, when community property is lost to third parties, the spouse last in possession has the burden of explaining the occurrence. If an adequate explanation is made, the loss is shared. If the explanation is insufficient, the loss is charged to the spouse last in possession. Trial courts frequently reject vague explanations of the disposition of community assets as attempted in *Reaney*, but it is unusual to require documentary evidence as in *Valle*. A general explanation that “I spent it” was rejected in *Linton v. Linton*, 303 P.2d 905 (Idaho 1956), a case in which the sum involved was \$20,000. It may be possible, however, to account for substantially lesser amounts through general testimony that the money was spent on basic living expenses. Such testimony has been accepted with regard to small amounts, such as \$470. *Cohen v. Cohen*, 164 Cal. Rptr. 672 (Ct. App. 1980); *Reppy & Samuel*, *supra* § 4.9, at 248–49.

In *Shreve v. Shreve*, No. 91-0635, 1991 WL 285884 (Wis. Ct. App. Nov. 5, 1991) (unpublished opinion not citable per section 809.23(3)), the court of appeals considered a related problem. While the divorce was pending, the husband incurred what the court found to be unnecessary and unreasonable debts. The court found that in so doing, the husband had intentionally depleted the couple’s divisible property. The court held that to remedy that misconduct, it is appropriate to assign debts to the party who has intentionally squandered the divisible property.

➤ **Comment.** It is unreasonable to expect a spouse to account for each item of income and each disbursement over the entire term of a marriage. To require such detailed accounting would in effect treat the spouse as a trustee and impose a burden beyond that reasonably to be expected from married individuals. *See Williams v. Williams*, 92 Cal. Rptr. 385 (Ct. App. 1971). Consistent with decisions in other community property jurisdictions, in Wisconsin the duty to account with regard to necessary records should be interpreted to accord with reasonable expectations of married individuals. *See infra* § 8.12.

A Wisconsin Court of Appeals case dealt with a divorcing spouse who lost \$45,000 while engaging in the investment practice of day

trading. *Derr v. Derr*, 2005 WI App 63, 280 Wis. 2d 681, 696 N.W.2d 170. The court held that the circuit court properly treated this loss as a wasted asset for purposes of the property division. The court did not determine which party had the burden of proof to prove the asset had been wasted. However, the court indicated that the spouse who lost the money had control of all the information pertinent to the question of waste and, thus, had an obligation to provide complete answers as to disposition of the funds.

## 5. Related-party Transactions [§ 4.33]

Questions of good faith may arise in related-party transactions. Transfers between family members must be analyzed to determine whether they are gift transactions and, if not, whether adequate consideration was received. If the transfer was not a gift and adequate consideration was not received, the facts may establish that the obligation of good faith was breached. See *Byrd v. Blanton*, 197 Cal. Rptr. 190 (Ct. App. 1983).

In the other community property states, gifts intended to defraud a spouse are found unfair, and the court may award exemplary damages. This was done in *Logan v. Barge*, 568 S.W.2d 863 (Tex. App. 1978). The husband in this case operated a general merchandise store in Texas until a few years before his death. During his lifetime, he kept large cash balances in a safe in the store, and from these funds he made large cash gifts to his children and grandchildren, without his wife's knowledge. The total amount transferred was \$245,820.72. The wife sought recovery of her community interest and exemplary damages from the gift recipients. The court found a conspiracy to transfer funds to the wife's detriment and awarded the reimbursement of one-half of the improperly given community cash, as well as exemplary damages. In Wisconsin, a conspiracy of this nature should be found to violate the good-faith obligation. The gift remedy may also apply.

A presumption of fraud may arise when one party produces facts that cast serious doubt on a transaction's validity. *Thompson v. Thompson*, 411 So. 2d 699 (La. Ct. App. 1982), concerned the conveyance of real property the parties purchased during the marriage. The parcel was community property. During the marriage, the husband allegedly sold the property to his sister. The wife later learned of the transfer and filed suit to have the conveyance set aside as fraudulent. To support her

position, she introduced the transcript from a previous court proceeding involving alimony in which the husband testified that he still owned the property and that his income in the year the sale allegedly occurred was only \$400, although the sale price was stated as \$20,000 in cash. The court held that the sale had no substance whatsoever, and the sale was set aside.

## **C. Gifts [§ 4.34]**

### **1. To a Third Party [§ 4.35]**

#### **a. General Rules [§ 4.36]**

Section 766.51(4) permits a spouse with management and control powers to make gifts of marital property assets to third persons. The management and control provision is unrestricted. *See* Wis. Stat. Ann. § 766.51(4) Legis. Council Committee Supplemental Notes Relating to 1985 Act 37 (West 2009). However, the Act has a specific provision, section 766.53, relating to recovery by the other spouse, which states that a spouse acting alone may give marital property assets to a third person only if the value of the marital property assets given does not “aggregate more than either \$1,000 in a calendar year, or a larger amount if, when made, the gift is reasonable in amount considering the economic position of the spouses.” If a gift does not comply with section 766.53, the other spouse has a remedy—a right of recovery. *See* Wis. Stat. § 766.70(6). The right of recovery applies to all gifts, including gifts to relatives or charities. If “both spouses act together in making the gift,” then the remedy is not available. Wis. Stat. §§ 766.53, 766.70(6).

➤ **Comment.** As originally enacted, section 766.51(4) stated that “[t]he right to manage and control marital property permits gifts of that property *only to the extent provided in s. 766.53*” (emphasis added). The 1985 Trailer Bill amended the statute to read, “The right to manage and control marital property permits gifts of that property, subject to remedies under this chapter.” Section 766.53 was not harmonized with the change in section 766.51(4) made by the 1985 Trailer Bill. Read alone, section 766.53 appears to grant a spouse management powers only for gifts within the amount limitations specified in that section. This reading is not correct. Each spouse has

the unlimited power to make gifts of marital property assets. *See* Wis. Stat. § 766.51(4).

The Act contains no limitation on a spouse's right to make gifts of his or her individual property or predetermination date property. This includes predetermination date property that would have been marital property if the Act had been in effect when the asset was acquired, property that thus would be subject to the deferred marital property election at death. *See infra* § 8.45. There is also no limitation on transfers in satisfaction of any debts, whether or not in the interest of the marriage or the family. Obligations of support are debts, and the gift provisions thus do not apply. *See infra* § 6.5.

Section 766.53 provides special valuation rules for two types of assets:

1. *Life insurance.* If the property transferred is a marital property life insurance policy (whether or not it is on the life of a spouse), it is valued at the amount that would have been payable under the policy if the insured had died when the gift was made. (The statute is unclear about this rule's application to the entire policy if only part of the policy is classified as marital property.)
2. *Retained interests.* If the donor spouse retains an interest in a marital property asset given to a third party, the gift is valued at its full value without consideration of the retained interest or any interest donated to the other spouse.

An absolute value is used in the above two situations because the actual value depends on numerous factors, including the health of the insured or donor, and the amount given often substantially exceeds the interpolated-terminal-reserve value or the value of the remainder interest.

A transfer of marital property during divorce proceedings is subject to the Act's remedies under section 766.70 rather than under chapter 767 if the proceedings are terminated by the death of one of the spouses. In *Socha*, 204 Wis.2d 474, the parties were involved in a divorce proceeding. The family court commissioner had entered two orders, one restraining the parties from disposing of assets and the other requiring each party to maintain in force all insurance. During the pendency of the divorce proceeding, the husband changed the beneficiary of his accidental life and group life insurance policies from his wife to his son.



Both policies were marital property. The husband died before the divorce was concluded, and therefore the parties were legally married at the time of the husband's death. The circuit court concluded that the husband had violated his duty of good faith and transferred assets in violation of court orders. The court placed a constructive trust over the entire proceeds, minus the \$1,000 the husband was authorized to give to a third party. On appeal, the court of appeals reversed the circuit court. Chapter 767 only applies when a divorce proceeding is pending. In this case, the husband's death terminated the divorce action, and therefore the wife's rights should have been determined pursuant to the Act's remedies provision. The court of appeals concluded that the proceeding was at law and not at equity.

➤ **Query.** Does a gift occur if the surviving spouse does not exercise the deferred marital property election? Section 861.10(3) expressly provides that the failure of a spouse to make the deferred marital property election is not a gift to the decedent spouse's estate or the party who would have been responsible for contribution.

#### **b. Reasonable Amount [§ 4.37]**

Courts in other community property states have considered what amount constitutes a reasonable gift. *De Funiak & Vaughn, supra* § 4.29, at 297–304. Their decisions should be helpful in determining the amount of marital property assets that may be given by one spouse acting alone to a third party without bringing into operation the recovery remedies. For example, *Horlock v. Horlock*, 533 S.W.2d 52 (Tex. App. 1975), concerned a husband's gifts to his daughters from a previous marriage. The gifts totalled \$131,517, and were made from community property during the parties' six-year marriage. The gifts ranged in value from \$3,000 to \$6,000 per year per donee, plus an amount equal to the \$30,000 lifetime federal gift tax exclusion then in effect. The wife challenged these gifts in the divorce proceeding. The husband and his accountant testified that reducing income taxes was the motivation for making the gifts. On the wedding date, the husband had property with a net value of approximately \$1 million. Throughout the marriage, the value of spouses' total assets exceeded \$1 million, and at dissolution, the spouses owned properties with a net value of approximately \$3 million to \$4 million.

The Texas court held that the spouse making a gift had the burden of proving that the gift was fair and not a constructive fraud. In determining whether the gifts in this case constituted a constructive fraud, the court considered three primary factors: (1) the size of the gift in relation to the total size of the community estate, (2) the adequacy of the assets remaining to support the spouse in spite of the gifts, and (3) the relationship of the donor to the donee. The court found that the gifts at most constituted approximately 13% of the total assets, the remaining community funds were sufficient to provide for the wife's needs, and the donees were the natural objects of the husband's bounty; thus, the court held that the gifts were fair and not a constructive fraud. *See also Marshall v. Marshall*, 735 S.W.2d 587 (Tex. App. 1987).

In Wisconsin, section 766.53 provides that a gift of more than \$1,000 to a third party by one spouse acting alone is not subject to the recovery statute if the gift is reasonable in amount, "considering the economic position of the spouses." In *Horlock*, the court looked at the amount of the community property as well as the separate property owned by the husband when the gifts were made. Apparently, the Wisconsin statute adopts the *Horlock* approach, and thus the spouses' marital property assets *as well as* their individual property and predetermination date property assets are considered. Arguably, then, a gift of marital property assets could be found reasonable in amount if a donor spouse has substantial nonmarital property assets and the marital property assets are significantly less. In such a case, however, it may be a breach of the obligation of good faith for the donor spouse to use marital property assets instead of nonmarital property assets for the gifts. *See supra* § 4.30.

The third factor in *Horlock* permits consideration of the relationship between the donor and the donee. This consideration would assist a spouse in avoiding a successful challenge based on the recovery statute if, for example, he or she used marital property funds to provide support, including support for post-high school education, to a child 18 or older from a prior marriage.

### **c. Date Gift Complete [§ 4.38]**

Under the Act, a gift is complete for property law purposes when the gift is made rather than when the statute of limitation for remedies expires. *See* Wis. Stat. Ann. § 766.51(4) Legis. Council Committee

Supplemental Notes Relating to 1985 Act 37 (West 2009). As to when a gift is complete for tax law purposes, *see* chapter 9, *infra*.

#### **d. Transactions Affected [§ 4.39]**

Section 766.53 on its face applies to all gifts of marital property assets. However, it may not apply to all gratuitous transfers under which marital property assets are transferred to third parties.

Several types of gratuitous transactions may not be affected by section 766.53. For instance, are enforceable charitable pledges superior to a spouse's remedy? Initially, such a pledge is a gift. If the pledge is not paid, however, it can be enforced by the donee under some circumstances. Richard A. Lord, *Williston on Contracts* § 8.4, 5 (4th ed. 1992). If the pledge is enforceable and can be reduced to a judgment, it is unclear whether the transaction should be analyzed as a gift or a contract. If it is analyzed as a contract, the issue is to determine the type of debt and then determine the property available for satisfaction. *See* Wis. Stat. § 766.55. However, if the pledge is analyzed as a gift and is paid from marital property funds, it appears that the nondonor spouse is not deprived of a remedy against the donee charity. This is true even if the spouse's promise could be enforced under the doctrine of promissory estoppel—for example, if the promise caused other donors to make gifts in reliance upon the spouse's pledge. 31 C.J.S. *Estoppel and Waiver* § 116 (2008); *see Bank of California v. Connolly*, 111 Cal. Rptr. 468 (Ct. App. 1973); Reppy & Samuel, *supra* § 4.9, at 239. Thus, the transaction may be enforced if the contract approach is used and may be subject to a remedy if the gift analysis is used.

➤ **Query.** Is a remedy available under section 766.53 if transfers are made by a sole proprietorship to a charity? For example, if the nonmanaging spouse can establish that for a period of years the other spouse's sole proprietorship made contributions in excess of \$1,000 to a charitable organization such as United Way, would these contributions be subject to an action by the nonmanaging spouse for recovery? Would evidence that the contributions were a legitimate business expense free the transfers from the statutory gift limitations? The better rule appears to be that gifts to a charitable organization or to political entities by a business or under a business motive are not subject to the provisions of section 766.53.

The Wisconsin Court of Appeals has considered whether a gift of marital property funds by the spouse of a lobbyist to an elected official outside the window within which the lobbyist was allowed to make the contribution violated a state statute regulating the conduct of lobbyists. *Katzman v. State Ethics Bd.*, 228 Wis. 2d 282, 596 N.W.2d 861 (Ct. App. 1999). In this case, the State Ethics Board sought to depose the spouse to determine why she made the contribution, and the Board took the position that if the contributions were made at the suggestion of the lobbyist, they would violate the statute. The circuit court enjoined the board from making this investigation, and the court of appeals affirmed. The court observed that the only relevant issue was whether the spouse was using the individual property of the lobbyist, and held that the spouse had a right to give marital property funds to whomever the spouse wanted, whenever the spouse wanted, and after such consultation as the spouse desired.

Finally, under section 766.53 there is a question whether a spouse's *voluntary* payment of a debt falls within the scope of the remedy available for gifts when the debt is otherwise unenforceable because the statute of limitation has run or the debt has been discharged in bankruptcy. Courts have recognized that a moral obligation to the recipient may remain. Washington courts have held that that state's restriction on gifts does not apply. *Catlin v. Mills*, 247 P. 1013 (Wash. 1926). *But see Gannon v. Robinson*, 371 P.2d 274 (Wash. 1962) (holding that attempted revival of debt after bankruptcy was not for benefit of community). Similarly, in Wisconsin this type of transaction may be found to be outside the scope of section 766.53 and subject only to the obligation of good faith. With regard to a guarantee of an indebtedness, *see* sections 4.59 and 6.22, *infra*.

#### **e. Gift from Commingled Account [§ 4.40]**

Questions about the gift's source are raised if one spouse acting alone makes a gift from a commingled account that includes nonmarital and marital property funds. By analogy to the duty to provide an accounting, *see supra* § 4.32, the donor spouse generally should have the burden of tracing the source of funds used. If the donor spouse is unable to establish the source, it appears that the gift should be presumed to have been made from his or her nonmarital property funds. *See supra* § 3.16. On the other hand, in *Succession of Ratcliff*, 24 So. 2d 456 (La. 1945), the court stated that absent an intent to use separate property, gifts should

be charged to the community. Consistent with *Ratcliff*, in Wisconsin it is anticipated that if spouses act together in making a gift from a commingled account, the gift should be presumed made from marital property funds.

#### **f. Remedies [§ 4.41]**

If a gift is found to have exceeded the amount authorized under section 766.53, the nondonor spouse has a right of recovery. Wis. Stat. § 766.70(6)(a). If a gift is excessive, some community property states consider the gift void, and others consider it voidable. Reppy & Samuel, *supra* § 4.9, at 239–40. Wisconsin has clearly selected the latter approach.

Section 766.70(6)(a) permits a nondonor spouse to bring an action against the donor spouse or the donee to recover either (1) the property or (2) a compensatory judgment equal to the amount by which the gift exceeded \$1,000 or a reasonable amount, whichever is greater. Allowing recovery of the property permits nullification of the entire transaction, including the amount that would have been reasonable. Thus, if a spouse gives a house worth \$50,000 to a child, and the court determines that only a \$25,000 gift would have been reasonable, the nondonor spouse has the right to recover either the entire house or a compensatory judgment of \$25,000. The nondonor spouse may bring action against the donor spouse, the gift recipient, or both. Wis. Stat. § 766.70(6)(a). Either recovery would be classified as marital property. If recovery occurs after a dissolution or after the death of either spouse, the recovery is limited to 50% of the recovery that would have been available if the recovery had occurred during marriage. *Id.*

In addition to bringing an action to recover the property under section 766.70(6), a spouse may challenge a gift on the ground that the gift was made in violation of the obligation of good faith. *See* Wis. Stat. § 766.15(1); *see also infra* § 8.18.

#### **g. Requirements to “Act Together” [§ 4.42]**

Section 766.53 provides that a gift is subject to the remedies of section 766.70(6) unless “both spouses act together in making the gift.” The Act does not define what constitutes acting together, and the

comment to UMPA section 6 is not of assistance. The comment does, however, state that the provision addresses the concern that a gift will defeat the other spouse's interest in the donated property. If a nondonor spouse approves a gift, the concern addressed by the provision is satisfied. Thus, almost any form of approval by a nondonor spouse should suffice, although affirmative approval, as opposed to mere knowledge, is necessary. Knowledge only shortens the statute of limitation. *See* Wis. Stat. § 766.70(6)(a).

Consistent with the Act's purposes, Wisconsin should recognize oral approval as constituting acting together. Similarly, approval given after a gift is made also should suffice and should be retroactive to the time of transfer. Wis. Stat. Ann. § 766.53 Legis. Council Committee Supplemental Notes Relating to 1985 Act 37 (West 2009). The Act does not require actual joinder by the spouses before or at the time of the gift transfer. *Cf. infra* § 4.47.

## 2. To a Spouse [§ 4.43]

The Act expressly permits spouses to reclassify their property by gift. *See* Wis. Stat. § 766.31(10). When spouses make gifts of property to each other, section 766.53 does not apply because the gift is not to a third party. One spouse acting alone may reclassify his or her individual or predetermination date property assets as marital property assets or as the individual property assets of the other spouse. *See* Wis. Stat. §§ 766.31(10), .51(1)(a). Likewise, one spouse acting alone with management powers may reclassify marital property assets as the individual property assets of the other spouse. *See* Wis. Stat. §§ 766.31(10), .51(1), (4).

Joinder is not required to effect these transactions. Wis. Stat. § 766.31(10); *see also infra* §§ 4.44–.48. In a gift between spouses, however, both spouses participate. Although only one spouse is the donor, the donee must accept delivery of the property for it to be a completed gift.

➤ **Comment.** It is not always clear whether a completed gift has occurred. For example, if a husband takes 100 shares of XYZ Corporation stock that is his individual property and reregisters the certificate in his name alone “as marital property,” has a gift occurred? Was there delivery and acceptance? As a further example,

if a husband and wife own an asset as tenants in common and reregister the title “as marital property,” have they reclassified the asset by gift? Before and after the change, they both owned an undivided one-half interest in the entire asset. What did they give? The Act does not provide an answer. The best answer seems to be that a gift occurred to the extent required for a reclassification under section 766.31(10). Until these issues are resolved, parties may wish to use a deed of gift or a marital property agreement to ensure that reclassification has occurred.

*State v. Baugh*, No. 93-1200-CR, 1994 WL 20071 (Wis. Ct. App. Jan. 26, 1994) (unpublished opinion not citable per section 809.23(3)), concerned one spouse’s theft of tangible property in the possession of the other spouse. At issue was whether the classification of the property had been changed by gift. The husband entered his estranged wife’s apartment and took certain items of her clothing and a radio. The husband was on bail, and his release was conditioned on his not engaging in any criminal activity. He was arrested and charged with theft and bail jumping. The husband acknowledged that he took the items but claimed the assets were classified as marital property and that he could not be convicted of stealing property in which he had an ownership interest. The wife testified that the items had been given to her and thus were her individual property. The jury determined that the items were the wife’s individual property and convicted the husband of bail jumping. The court of appeals held that the jury’s finding as to ownership of the items was reasonable and obviated the need for discussion of the husband’s contention that the items were marital property.

## **D. Joinder: Concurrent Management [§ 4.44]**

### **1. In General [§ 4.45]**

Wisconsin spouses are not required to act together in acquiring marital property assets. If a marital property asset is held in the names of both spouses other than in the alternative, the spouses must act together in managing and controlling the asset. Wis. Stat. § 766.51(2). However, acting together is probably only required for conveyances and for leases of more than one year, not for routine administrative management. *See infra* § 4.46.

The requirement that spouses act together is found in the gift statute, section 766.53, *see supra* § 4.42, and also in the management statute, section 766.51(2). It appears that the requirement that spouses act together has different meanings in the different statutes. In the gift statute, simultaneous action is not required and subsequent consent is permitted. Wis. Stat. Ann. § 766.53 Legis. Council Committee Supplemental Notes Relating to 1985 Act 37 (West 2009). In the management statute, acting together probably must entail signing the conveyance or lease in the same manner as for the conveyance of a homestead. *See infra* § 4.47.

## **2. Transactions Requiring Spouses to Act Together**

### **[§ 4.46]**

Many other community property states require joinder for the acquisition, sale, or encumbrance of real property and certain other community assets. Reppy & Samuel, *supra* § 4.9, at 215–41. In Wisconsin, joinder is required in only two situations. First, conveyance of a homestead requires both spouses either to sign the conveyance or to join in it by separate conveyance. Wis. Stat. § 706.02(1)(f). Second, the right to manage and control a marital property asset that is held in both spouses' names other than in the alternative requires the spouses to act together. Wis. Stat. § 766.51(2); *see also infra* ch. 5. Neither of these provisions applies to the acquisition of property.

With regard to a homestead, both spouses must sign a conveyance that alienates any interest of a spouse in the homestead, whether or not the homestead is classified as marital property. Wis. Stat. § 706.02(1)(f). Exceptions are made for conveyances of homesteads between spouses and for purchase money mortgages if only one spouse is the purchaser. *Id.* A spouse can waive homestead rights in a premarital agreement. *Jones v. Estate of Jones*, 2002 WI 61, 253 Wis. 2d 158, 646 N.W.2d 280.

With respect to marital property assets held in the names of both spouses other than in the alternative, the statute only applies to marital property assets held (already owned) by the spouses. Wis. Stat. § 766.51(2). Thus, joinder or acting together is not required when an asset is acquired even if title will be taken in both names other than in the alternative.



When a marital property asset is held in the names of both spouses other than in the alternative, what specific transactions require both spouses to act together? Section 766.51(2) does not expressly provide any exception to its requirement that spouses act together, and the statute has no accompanying notes. The comment to section 5 of UMPA states: “If ‘and’ is used in the concurrent title, *both* spouses manage and control, and joinder is required to discharge management and control functions.”

Must both spouses act together to convey marital property real estate titled in the names of both spouses other than in the alternative? *Conveyance* is defined as a written instrument evidencing a transaction “by which any interest in land is created, aliened, mortgaged, assigned or may be otherwise affected in law or in equity.” Wis. Stat. §§ 706.001(1), 706.01(4). The term is also defined in other sections of the Wisconsin Statutes. *See, e.g.*, Wis. Stat. §§ 77.21(1), 178.01(2)(c), 243.04. A conveyance is the most significant management transaction, and it is likely, as with a homestead, that both spouses must act together. Likewise, a lease for more than one year of a marital property asset held by spouses other than in the alternative must meet the standards for a conveyance and should require the spouses to act together. *See* Wis. Stat. § 704.03. Leases for one year or less may not require the spouses to act together, because fewer formalities are involved and the lease can be oral.

For some other management transactions involving property held in the names of both spouses other than in the alternative, it is not likely that both spouses must act together. For example, if spouses own their residence in both names other than in the alternative and wish to contract with a third party to paint the house, does this contract require both spouses to act together? In determining the situations requiring spouses to act together, the joinder cases in other community property jurisdictions may be of assistance.

In *Meltzer v. Wendell-West*, 497 P.2d 1348 (Wash. Ct. App. 1972), the issue was whether one spouse could hire a contractor to remodel the community residence when state law created an automatic mechanic’s lien in the event of nonpayment. The court held that one spouse acting alone could make such a contract even though a lien could result. In Wisconsin, this holding may not be consistent with the rule that one spouse may not create a security interest in or otherwise encumber a marital property asset in connection with an application for extension of credit unless that spouse otherwise has management and control rights

over the asset. See Wis. Stat. § 766.51(1m)(b); see also *infra* ch. 5. However, it seems appropriate that one spouse should be able to enter into such contracts and that any resulting lien should be outside the scope of the credit prohibition and the “acting together” requirement. This conclusion can also be based on an apparent-agency analysis.

In *Reimann v. United States*, 315 F.2d 746 (9th Cir. 1963), the court considered whether under Idaho law one spouse acting alone could contract with the U.S. Department of Agriculture under the soil-bank program not to plant any crops on community property real estate. The court held that the spouse’s action neither created an encumbrance nor violated the requirement that spouses act together.

The rule in Wisconsin probably should permit one spouse acting alone to execute certain contracts regarding at least some uses of marital property assets held in the names of both spouses other than in the alternative. Each spouse acting alone should be able to enter into contracts for the routine management and maintenance of marital property assets even though the property is held in a form requiring the spouses to act together. The extent to which the managing spouse is subject to the duty of good faith and the remedies available to the nonmanaging spouse should be sufficient protection.

In some situations, the actual ownership of property may be changed without spouses acting together. This issue was considered in *Janes v. Le Deit*, 39 Cal. Rptr. 559 (Ct. App. 1964). The husband acquiesced in the placement of a fence on what was assumed to be the boundary between a community property parcel and an adjoining parcel. Actually, the fence encroached 400 feet onto the community land, and under California law, acquiescence in the fence had the effect of shifting the boundary. The court held that even though the wife had never seen the property and had no knowledge of her husband’s acquiescence, the neighbor acquired the 400-foot strip of community realty. The court held that the joinder statute was inapplicable because no instrument of conveyance was involved.

### **3. Satisfaction of the Acting-together Requirement** **[§ 4.47]**

When spouses must act together, what is required? The notes to the Act and the comments to UMPA are not of assistance.

Besides section 766.51(2), the only other statute using the “act together” language is the gift statute, section 766.53. For gifts, the spouses are not required to act simultaneously, and a subsequent consent is sufficient. Wis. Stat. Ann. § 766.53 Legis. Council Committee Supplemental Notes Relating to 1985 Act 37 (West 2009). For a gift, it is probably sufficient if the subsequent consent is oral.

The gift standard may not apply in situations in which acting together is required in a conveyance or a lease for more than one year. With those transactions, there is a document of title, and the third party should know that bona fide purchaser status is obtained only if the property is acquired or leased from a spouse or spouses having the right to manage and control the property. See Wis. Stat. § 766.57(3). Thus, the third party should insist that both spouses sign the lease or conveyance as part of the closing.

The gift standard for acting together may be appropriate, however, for other management transactions for which spouses are required to act together. For example, if both spouses must act together in contracting to paint their house, then subsequent and oral consent to the contract should be sufficient.

#### **4. Consequences of Spouses’ Failure to Act Together [§ 4.48]**

If spouses must act together but do not, the final issue is whether the transaction is void or voidable. In Idaho, Arizona, and New Mexico, if joinder is required and does not occur, the transaction is wholly void. Reppy & Samuel, *supra* § 4.9, at 223. This is the result in Wisconsin if both spouses do not join in a conveyance of a homestead. See Wis. Stat. § 706.02. But see *Jones*, 2002 WI 61, 253 Wis. 2d 158 (holding that waiver of homestead-conveyance protection in premarital agreement was valid). In Louisiana, Washington, and California, the transaction is merely voidable and may be voided only by the nonjoining spouse. Reppy & Samuel, *supra* § 4.9, at 223. This is the result in Wisconsin if an excessive gift is made and the spouses do not act together. See Wis. Stat. § 766.70(6).

Neither the Act nor UMPA indicates the result for other situations when spouses are required to act together and fail to do so. The failure to act together could be found merely to authorize an interspousal remedy

and to have no effect on the third party. *See infra* § 8.18. This result is unlikely, at least in cases involving conveyance of an interest in property, in which a third party should know that both spouses are required to act together and that, if they fail to do so, the third party is not a bona fide purchaser. Whether a transaction is void or voidable, it is likely that only the nonjoining spouse can raise the issue.

Finally, even when the rule is that the transaction is voidable if the joinder requirements are not met, it has been held in some circumstances in other community property states that a spouse can be estopped from challenging the transaction. *Reid v. Cramer*, 603 P.2d 851 (Wash. Ct. App. 1979), concerned a husband who contracted to purchase a tract of land, signing a promissory note as earnest money, and then attempted to repudiate the agreement, arguing that the contract and note were not binding because his wife had not joined in the transaction. The court held that the community is estopped to deny a liability resulting from the failure of one spouse to join a transaction when (1) one spouse permits the other to carry out the transaction, (2) both have a general knowledge of the transaction, and (3) both are ready to accept the benefits that may come from the transaction. In *Reid*, the court held that the wife generally knew of the transaction and was ready to accept the benefits, and thus she was estopped from disaffirming the transaction. *But see Smith v. Stout*, 700 P.2d 343 (Wash. Ct. App. 1985) (finding that wife was not ready to accept benefits of transaction in which she did not participate because she had already signed an agreement to sell property at issue to other people).

In Wisconsin, the facts in some cases may justify estoppel when spouses have not acted together. However, mere knowledge of a transaction may not be sufficient. In the gift context, knowledge only shortens the statute of limitation. *See* Wis. Stat. § 766.70(6)(a). Knowledge is not acting together and may not be sufficient to raise the equitable bar of estoppel.

## **E. Civil Procedure [§ 4.49]**

### **1. Parties [§ 4.50]**

#### **a. In General [§ 4.51]**

An important management and control right is the right to institute an action to recover for damage to marital property assets or for personal injuries resulting in a loss of marital property income. *See* Wis. Stat. § 766.01(11). The corollary is that the right to defend an action exists if the judgment in the action can be satisfied from marital property assets. *Id.* The civil procedure statutes that apply to actions involving marital property assets do not distinguish between actions based on contract and actions arising from a tort.

With regard to such management rights, the first issue concerns who is the proper plaintiff in an action affecting marital property. Under the Act, resolution of this issue can be approached in either of two ways depending on (1) whether the cause of action is an incident of ownership of an asset or (2) whether once an asset has been damaged, the cause of action is an intangible separate right.

Under the first approach, which focuses on the cause of action as an incident of ownership, management and control of the cause of action is based on how the marital property asset itself is held. For example, if an automobile classified as marital property and held in one spouse's name is damaged in an accident caused by a third party, a cause of action arises with respect to that damage. The Act does not indicate whether this cause of action is an incident of ownership of the automobile and is thus also held by the spouse who holds the automobile. If the cause of action is an incident of ownership of the automobile, it is considered held by that spouse, and the Act limits the right to bring the action to the holding spouse. If the automobile was instead held in the names of both spouses other than in the alternative, and the cause of action is considered an incident of the property, then management and control rights over the cause of action would require both spouses to act together. *See* Wis. Stat. § 766.51(2). If the cause of action retains the management characteristics of the asset, both spouses apparently must act together to commence an action for relief.

This approach is supported by the definition of *management and control*, which includes “the right to ... institute or defend a civil action regarding ... property.” See Wis. Stat. § 766.01(11). Under this analysis, some causes of action, such as those for personal injury or libel and slander, are not attributable to any asset, and thus, if the recovery would be marital property, either spouse could bring the action. (The limitation on who may act as plaintiff does not affect who may be named as defendant, because if a recovery from marital property assets is appropriate, it can be satisfied from marital property assets held by either spouse.)

The second approach focuses on the cause of action itself as a separate asset. The first question under this approach is whether the recovery would be marital property. If so, the cause of action would be an asset that was not held by either spouse. See Wis. Stat. § 766.01(9). As such, either spouse acting alone could manage and control the asset and thus institute the action. Wis. Stat. § 766.51(1)(am). Under this approach, then, either spouse acting alone may recover for injury to a marital property asset, regardless of how the asset was held. However, this is probably not the correct analysis.

➤ **Comment.** Under both approaches, section 766.51(1)(f) appears to be limited to causes of action created by other statutes, such as those governing worker’s compensation, wrongful death, and loss of consortium. Section 766.51(1)(f) provides that a spouse acting alone may manage and control a claim for relief vested in that spouse by law other than the Act. This provision is in UMPA, but its scope is undefined. It does not, however, appear to take the analysis of the proper party for most causes of action outside the management and control analysis of the Act.

The Act changed Wisconsin’s rules of civil procedure to reflect the additional ownership interest in marital property assets and the new obligations that may be satisfied from marital property assets. Section 803.04(3) provides that “[i]n an action affecting the interest of a spouse in marital property, as defined under ch. 766, a spouse who is not a real party in interest or a party described under s. 803.03 may join in or be joined in the action.” Thus, in all actions affecting a spouse’s interest in a marital property asset, both spouses thus are permissive parties either as plaintiff or as defendant. According to the Legislative Council notes on the creation of section 803.04(3), “The provision is intended to clarify that, at the initial stages of an action affecting a spouse’s interest in

marital property, both spouses may sue or both spouses may be sued.” Wis. Stat. Ann. § 803.04 Legis. Council Notes—1985 Act 37, § 152 (West 1994). The Legislative Council notes do not mention whether either or both spouses hold the marital property asset involved in the action. The notes imply that either spouse could maintain an action to recover for damage to a marital property asset, even if the asset is held in only one spouse’s name. The notes continue:

It is recognized by the Special Committee that it may be desirable to deal more specifically in the statutes with the issue of when a spouse is a proper party plaintiff or defendant in an action affecting marital property. However, the Special Committee concluded that ch. 766 and the current rules of civil procedure provide general guidance in this regard. More detailed rules, if necessary, are best left to future legislation.

*Id.*

➤ **Comment.** To commence an action, there must be a real party in interest, and whether there is such a party is probably determined from an analysis of whether and how the marital property asset involved is held by a spouse. Since section 803.04(3) deals only with permissive joinder of parties, it should not be construed to authorize a spouse acting alone to commence an action when the underlying marital property asset that is the subject of the litigation is held solely in the other spouse’s name. Likewise, both spouses should be required parties to maintain an action involving a marital property asset held in both names other than in the alternative. *See infra* § 6.54.

### **b. Spouse as Plaintiff [§ 4.52]**

The Wisconsin rules as to proper party under chapter 803 when a spouse is a plaintiff will probably be applied as follows:

1. A cause of action involving damage to individual or predetermination date property must be commenced by the spouse owning the property. The other spouse is not a proper party.
2. A cause of action involving a spouse who sustains a personal injury must be commenced by the spouse who sustained the injury because the recovery for pain and suffering is individual property. *See Wis.*

Stat. § 766.31(7)(f). Either spouse may commence an action for the portion of the asserted liability representing loss of income during marriage. *See* Wis. Stat. § 766.31(4), (7)(f).

3. A cause of action involving a marital property asset that is not held by either spouse or that is held by both spouses in the alternative may be commenced by either spouse. The other spouse is a permissive party.
4. A cause of action involving a marital property asset held by one spouse must be commenced by that spouse. The other spouse is a permissive party.
5. A cause of action involving a marital property asset held by both spouses other than in the alternative must be commenced by both spouses. If one spouse is disabled or absent, see section 4.58, *infra*.
6. A cause of action involving contract rights arising other than from property that is held (such as an action for breach of contract or loss of income from a contract), and for which the recovery would be marital property, is not held by either spouse and so may be commenced by either spouse.
7. Any other cause of action authorized by law, such as worker's compensation or loss of consortium, may be commenced by the spouse authorized by the statute involved. Wis. Stat. § 766.51(1)(f).

If a cause of action involving a marital property asset or contract right is commenced by one spouse, the defendant can move to join the other spouse because that spouse is a permissive party. *See* Wis. Stat. § 803.04(3). This rule helps ensure that all claims of both spouses against the defendant and arising from the transaction will be adjudicated in a single proceeding.

➤ **Example.** Assume that a wife sustains a personal injury in an automobile accident and the vehicle is her husband's individual property. Neither spouse acting alone can fully resolve all claims. The recovery for pain and suffering is the wife's individual property, the recovery for damage to the automobile is the husband's individual property, and the recovery for loss of income is marital property. If the action is commenced only by the wife and she settles the case and classifies the entire recovery as her individual property, is the



defendant protected from a subsequent claim by the husband for the loss of income? Has the wife breached her obligation of good faith?

➤ **Practice Tip.** When an action commenced by one spouse is being settled, the other party may wish to consider obtaining releases from both spouses. Joinder and releases from both spouses may be appropriate because the decision has claim preclusive effect only as to the issues actually and necessarily determined in the proceedings.

Because the rules summarized above are consistent with the rules in the other community property states, the decisions in those states will assist in applying the rules in Wisconsin.

The issue of proper plaintiff was addressed in *Amador v. Lara*, 603 P.2d 310 (N.M. Ct. App. 1979). The wife sustained personal injuries in an automobile accident. During the trial, the wife sought to introduce evidence to show that she and her husband lost income because she could no longer help him in his business. The trial court denied the admission of this testimony on the ground that the husband was not a party to the lawsuit and the wife could not properly seek his lost income.

The appellate court reversed, holding that the wife acting alone could bind the community. According to the appellate court, the husband was not an indispensable party in the case. The wife's injuries caused the loss of services to the community, and she was entitled to recover the full amount of the community's loss. The court agreed that it is best for both spouses to join in the prosecution of a claim for community damages. But the best method is not necessarily the only permissible method.

The converse occurs when one spouse's separate property is harmed and the other spouse attempts to recover for the loss. This situation was considered in *Carr v. Galvan*, 650 S.W.2d 864 (Tex. App. 1983). The husband sued an automobile dealer for damages that the defendant's service station caused to the wife's car, which was her separate property; the husband also sued for assault and battery by the station owner, which allegedly occurred when the husband complained about the damage. The court held that the cause of action for damages to the automobile was the wife's separate property; thus, the suit for such damages could not properly be pursued by the husband alone.

➤ **Comment.** The above result should also occur in Wisconsin. If the damaged asset is one spouse's individual or predetermination date property, only that spouse should be able to initiate an action. This result is consistent with common law rules that continue for predetermination date property. It should be immaterial whether the asset is potentially deferred marital property or whether, when a recovery occurs, any subsequent income from it is marital property.

### **c. Spouse as Defendant [§ 4.53]**

In all cases in which marital property assets can be reached to satisfy an obligation, the creditor may proceed against the obligated spouse, the incurring spouse, or both spouses. Wis. Stat. § 803.045(1). In addition, when an obligation either (1) arises from a duty of support owed to the other spouse or to a child of the marriage or (2) is incurred in the interest of the marriage or the family, Wis. Stat. § 766.55(2)(a), (b), a creditor may proceed against the nonobligated or nonincurring spouse alone only if the creditor cannot obtain jurisdiction in the action over the obligated or incurring spouse. Wis. Stat. § 803.045(2). However, after a judgment has been obtained, a creditor may proceed against either or both of the spouses to reach marital property assets available for satisfaction of the judgment. Wis. Stat. § 803.045(3); see *Bank One, Appleton, NA v. Reynolds*, 176 Wis. 2d 218, 500 N.W.2d 337 (Ct. App. 1993).

The Wisconsin rules as to proper party under chapter 803 when a spouse is a defendant will probably be applied as follows:

1. If a spouse defaults on a nonsupport and non-family-purpose obligation or on an obligation incurred before January 1, 1986, or before marriage, the creditor may maintain an action against the incurring spouse or against both spouses because marital property assets may be available for satisfaction. Wis. Stat. § 803.045. The nonincurring spouse has no personal liability.
2. If a third-party creditor has a cause of action against one spouse regarding an obligation in the interest of the marriage or the family or for tort liability, the creditor may maintain an action against the incurring spouse or against both spouses. Wis. Stat. § 803.045. This conclusion was adopted by a Wisconsin circuit court in *Rauen v. Kloth*, 87-CV-620 (Wis. Cir. Ct. Marathon County 1988). The nonincurring spouse has no personal liability. In addition, if the

creditor cannot obtain jurisdiction over the incurring spouse, the creditor may proceed against the nonincurring spouse alone. Wis. Stat. § 803.045(2).

*Bothe v. American Family Insurance Co.*, 159 Wis.2d 378, 464 N.W.2d 109 (Ct. App. 1990), concerned spousal liability for tort obligations resulting from an automobile accident in which the husband was driving a vehicle and the plaintiff was injured. The plaintiff commenced the action against the husband, the wife, and their insurance company. At the time of the accident, the spouses were living apart, and each had a separate liability policy with the same insurance company. The wife was not involved in the accident. The wife and her insurance carrier moved for summary judgment. The circuit court granted the motion and held that section 766.55(2)(cm) does not make an innocent spouse liable for any kind of tort committed by the other spouse.

On appeal, the plaintiff argued that the statute subjects an innocent spouse to liability for tort obligations by virtue of the tortfeasor's interest in the marital property assets of the innocent spouse. The court of appeals held that section 766.55(2)(cm) was not ambiguous, stating that "the statute does nothing to change the traditional concept of *liability* for the tort." *Id.* at 382. The statute "*protects* the innocent spouse's property from, rather than subjects it to, liability for the tortfeasor spouse's obligations." *Id.* Thus, the wife had no liability for her husband's tort, and therefore the plaintiff could not recover from the wife's liability insurance carrier. The insurance carrier had no duty to defend under the policy because there was no proper assertion that the insured was legally liable. Under the analysis in section 4.51, *supra*, the wife could have remained a party to protect her interest in marital property assets.

*Oil Heat Co. v. Sweeney*, 613 P.2d 169 (Wash. Ct. App. 1980), involved a situation in which a third party was permitted to proceed solely against the noncontracting spouse. The court held that since either spouse may manage community property, service of process on either spouse is permitted in an action involving a community obligation. This case was not, however, based on the same community property rules that exist in Wisconsin. In Washington, both spouses are jointly and severally liable for community obligations, while in Wisconsin, generally only the incurring spouse has personal liability and all marital property assets and the incurring spouse's nonmarital property assets are available

for satisfaction of a family-purpose obligation. See Wis. Stat. § 766.55(2)(b).

A separate issue that arises in civil and criminal litigation is the indigent's right to counsel. In *State v. Wing*, No. 91-0362-CR, 1991 WL 285874 (Wis. Ct. App. Nov. 7, 1991) (unpublished opinion not citable per section 809.23(3)), the defendant requested representation by a public defender. Although his wife had income and assets, the defendant asserted he had no interest in the assets because of their marital agreement. The validity of an unsigned copy of a purported agreement could not be established. The court considered the defendant's marital property interest in the assets held by the wife and denied his request for representation by a public defender.

If a third-party creditor of a spouse believes an action involving the spouses may reduce the assets available to satisfy the obligation, the creditor can intervene as a third party claiming an interest in the real and personal property. *Curda-Derickson v. Derickson (Sokaogon Gaming Enter. Corp. v. Curda-Derickson)*, 2003 WI App 167, 266 Wis. 2d 453, 668 N.W.2d 736.

## 2. Lien [§ 4.54]

Section 806.15(4) provides that a lien does not attach to property that is held solely by the spouse or former spouse of a judgment debtor

unless the spouse of the judgment debtor is a named defendant in the action for which judgment is rendered, the spouse of the judgment debtor is named in the judgment itself, the obligation is determined an obligation described in s. 766.55(2) and any of the following applies:

(a) With respect to property held by the spouse of the judgment debtor when the judgment is entered in the judgment and lien docket, the property is expressly determined available under s. 766.55 to satisfy the obligation.

(b) The property is acquired after the judgment is entered in the judgment and lien docket.

Thus, if an action is brought only against the incurring or obligated spouse, and a judgment is rendered against that spouse and is properly docketed, the judgment does not become a lien on marital property real estate then held only in the name of the judgment debtor's spouse.

Likewise, it may not become a lien on marital property real estate subsequently acquired solely in the name of the judgment debtor's spouse. *See infra* § 6.58. Thus, it is desirable to commence an action against both spouses.

If a judgment lien has attached to property that is exempt from execution on the judgment lien, a person with an ownership interest in the property may proceed under section 806.04 for declaratory relief if the owner of the judgment fails within 10 days after demand to execute a recordable release of the property from the judgment lien. Wis. Stat. § 806.15(5); *see infra* § 6.58. Property to which a judgment lien attaches under section 806.15(4)(b) that is not available under section 766.55 to satisfy the obligation for which the judgment was rendered is exempt from execution. Wis. Stat. § 815.205(1). A person with an ownership interest in the property may stay an attempt at execution on such property. Wis. Stat. § 815.205(2).

### **3. Proceedings in Aid of Execution [§ 4.55]**

The final step in managing a cause of action is either to obtain satisfaction of a judgment obtained or to defend against an attempt. The first step in many cases is to take a supplemental examination of the judgment debtor to ascertain the assets available to satisfy the obligations. Wis. Stat. § 816.03(1). The judgment creditor may also conduct a supplemental examination of the spouse of the judgment debtor. *Courtyard Condo. Ass'n v. Draper*, 2001 WI App 115, 244 Wis. 2d 153, 629 N.W.2d 38.

If a third party becomes a judgment creditor of a spouse, it may be necessary to levy execution on the judgment. *See* Wis. Stat. § 815.01. In connection with execution, section 815.18(8) provides that, in proceedings to enforce a judgment against a marital property asset on an obligation incurred in the interest of the marriage or the family, each spouse is entitled to and may claim the exemptions under section 815.18. *See infra* § 6.68. If the exempt property is limited to a specific maximum dollar amount, each spouse is entitled to one exemption. That maximum dollar amount may be either combined with the other spouse's exemption in the same property or applied to different property included under the same exemptions. The only exception to this rule is that the exemption for income may not be combined with the other spouse's exemption that

applies to that income. *See* Wis. Stat. § 815.18(8), (3)(h); *see also Bank One, Appleton*, 176 Wis. 2d 218.

In addition to enforcement by execution, enforcement may be by prejudgment attachment. *See* Wis. Stat. § 811.01. For purposes of the attachment statute, the term *defendant* is defined to include the spouse or former spouse of the defendant if the action against the defendant is in connection with an obligation described under section 766.55(2). Wis. Stat. § 811.001(1). *Property of his or her debtor and property of the defendant* are defined to include the marital property interest in an asset of the spouse or former spouse of the debtor or defendant if the action against the debtor or defendant is in connection with an obligation described in section 766.55(2). Wis. Stat. § 811.001(2). These definitions “reflect that a creditor may have reason to attach marital property in which a spouse has an interest even though the spouse is not personally liable to the creditor.” Wis. Stat. Ann. § 811.001(2) Legis. Council Notes—1985 Act 37, § 154 (West 2007). Section 811.03(1), providing for attachment based on a contract or judgment, enables the plaintiff to execute an affidavit stating that property of the defendant is available for satisfaction of the indebtedness. It is not necessary to assert that the defendant is indebted to the plaintiff. *See infra* § 6.65.

Enforcement may also be by garnishment after judgment is obtained. Section 812.01(1) authorizes any creditor to proceed against any person who is indebted to the creditor or who has property in his or her possession or control that is subject to the satisfaction of an obligation described under section 766.55(2). The term *defendant* is defined to include a judgment debtor or the spouse or the former spouse of a judgment debtor if the judgment is rendered in connection with an obligation described under section 766.55(2). Wis. Stat. § 812.01(1). Section 812.02(2e) provides that a plaintiff “may not commence any garnishment action affecting the property of a spouse who is not a defendant in the principal action unless the spouse is a defendant in the garnishment action.” *See infra* § 6.59. *Bank One, Appleton*, 176 Wis. 2d 218; *In re Possmore*, 156 B.R. 595 (Bankr. E.D. Wis. 1993). A creditor may proceed against either spouse alone or both spouses in the garnishment action to reach marital property (such as wages) available for satisfaction of the judgment. Wis. Stat. § 803.045(3); *Journal Sentinel, Inc. v. Schultz (In re Schultz v. Sykes)*, 2001 WI App 260, 248 Wis. 2d 791, 638 N.W.2d 76.

➤ **Historical Note.** The Legislative Council special committee that proposed the explanatory notes to the Act concluded that “s. 812.02(1)(b), which permits commencement of a garnishment action after an execution upon an in *personam* judgment is issuable, covers the situation; an in *personam* judgment does not necessarily imply personal liability.” Wis. Stat. Ann. § 812.01 Legis. Council Notes—1985 Act 37, § 156 (West 1994). Thus, the special committee concluded that no amendment to section 812.02(1) was necessary.

*State v. Zimmer*, No. 91-1553-CR, 1991 WL 319136 (Wis. Ct. App. Dec. 11, 1991) (unpublished opinion not citable per section 809.23(3)), concerned a husband who was convicted of a misdemeanor for his maltreatment of animals owned by the spouses. As part of the penalty for the offense, the circuit court ordered the husband to forfeit the animals. The husband objected to the forfeiture on the basis that his wife owned a one-half interest in the animals pursuant to the provisions of the Act. The court held that the husband lacked standing to assert his wife’s alleged interest in the property. The wife was found to have a remedy because she could seek to have her rights declared under the Act and could raise a constitutional due process claim if the forfeiture attempted to reach her property.

*First Wisconsin National Bank v. Peterson*, No. 91-0995, 1991 WL 319114 (Wis. Ct. App. Dec. 17, 1991) (unpublished opinion not citable per section 809.23(3)), concerned a deficiency judgment against one spouse. The wife had granted a mortgage to the bank on a property owned by her to secure a promissory note of her husband. When the husband defaulted on the promissory note, the bank brought an action to foreclose the mortgage. The circuit court issued a summary judgment granting the foreclosure and rendered a deficiency judgment against the wife personally in the event that the property sale proceeds did not fully satisfy the amount due on the promissory note. The court of appeals, citing section 6.21 of the original edition of the book (section 6.51, *infra*, in this edition), held that the granting of a deficiency judgment against the wife was not appropriate. The indebtedness could only be collected from the individual property assets of the incurring spouse and from all marital property assets. The court stated that “[t]he statute does not render the spouse who did not incur the debt personally liable for the debt of the incurring spouse.” 1991 WL 319114, at \*8.

*Kotecki v. Marek*, No. 93-0495, 1993 WL 404321 (Wis. Ct. App. Oct. 12, 1993) (unpublished opinion not citable per section 809.23(3)),

concerned the spouse's responsibility for attorney fees. The plaintiff, an attorney, had obtained a judgment against the wife for attorney fees. The wife's husband was not joined in that action. When the judgment was not satisfied, the attorney commenced a garnishment action against the husband, the husband's employer as garnishee, and the wife and obtained a default judgment against the employer. The husband moved to reopen the garnishment judgment and requested costs on the ground that the action was frivolous. The circuit court reopened and dismissed the default judgment and awarded the husband "frivolous attorney fees and costs."

The court of appeals reversed. The court found that the wife's obligation to the attorney was incurred in the interest of the marriage or the family. Sections 812.01(1) and 812.02(2e) permit a garnishment action against the employer of the nonobligor spouse who was not a party in the principal action if the spouse whose property is affected is a party named in the garnishment proceeding. The court then found that the employer was a proper garnishee because the employer had property in its possession that was subject to satisfaction of a family-purpose obligation. The court of appeals directed the circuit court to vacate its order and directed the employer pay the money owed to the attorney. The court of appeals also reversed the determination that the attorney's proceeding was frivolous.

#### **4. Statute of Limitation [§ 4.56]**

Procedural issues also arise when both spouses are obligated on an indebtedness and the statute of limitation has run against one spouse but not the other. May the claim be pursued against that one spouse? This issue was considered in *Roper v. Jeoffroy Manufacturing, Inc.*, 535 S.W.2d 706 (Tex. App. 1976). The husband and wife had signed a promissory note to a third party and subsequently defaulted in its payment. An action was brought against the husband and wife. The statute of limitation had run against the husband, but the wife had been out of the state, so the tolling statute permitted a suit against her. The court held that the suit could proceed against the wife.

This analysis of the statute of limitation when both spouses are personally liable seems to apply in Wisconsin. The statutory limitation on commencement of actions only bars an action against a party for whom the period has expired. See *Spellbrink v. Bramberg*, 245 Wis. 103,



13 N.W.2d 600 (1944); *Caswell v. Engelmann*, 31 Wis. 93 (1872). If there are several party defendants, the applicable statute may run for some and be tolled for others. *See* Wis. Stat. §§ 893.10–.23. If the plaintiff can proceed against one spouse, and if the obligation was incurred in the interest of the marriage or the family, the obligation can be satisfied from all marital property assets. Wis. Stat. § 766.55(2)(b). The nonmarital property assets of the spouse against whom the statute ran cannot, however, be reached to satisfy the indebtedness.

➤ **Note.** If only one spouse is personally obligated on the family-purpose obligation and the statute runs against that spouse, no action against the other spouse should be permitted. To commence an action, there must be an obligation. The liability of the nonobligated spouse is derivative of the incurring spouse's obligation, and if the statute of limitation runs against the incurring spouse, the obligation ends. *See infra* ch. 5 (claims statute at death).

## **F. Living Separate and Apart [§ 4.57]**

Management and control problems can arise when spouses are not living together. In Wisconsin, it is possible for one of the spouses living apart to seek a legal separation and obtain a property division. *See* Wis. Stat. §§ 767.02(1)(d), .255. A legal separation is a dissolution of the marriage, and thereafter the spouses do not acquire assets classified as marital property. *See* Wis. Stat. § 766.01(7). If the spouses have a legal separation, management rights change accordingly. Instead of seeking dissolution, a spouse can use the remedy provisions and request an order, under section 766.70(4)(a)5., that classifies all subsequently acquired property as the individual property of the acquiring spouse. *See infra* § 8.34. In most cases, however, no judicial relief is sought until one or both of the spouses commence an action for dissolution of their marriage.

In Wisconsin, living separate and apart, by itself, regardless of duration, does not change the classification of property or the management and control rights in property. This conclusion is consistent with UMPA, which emphasizes that the property rules track the status of spouses. UMPA § 1 cmt. 8; *see also Aetna Life Ins. Co. v. Bunt*, 754 P.2d 993 (Wash. Ct. App.), *rev'd in part on other grounds*, 754 P.2d 993 (Wash. 1988); *In re Estate of Osicka*, 461 P.2d 585 (Wash. Ct. App. 1969).

In some community property jurisdictions, an equitable analysis is made to determine whether a renunciation of the community has occurred when the spouses live apart. *See Togliatti v. Robertson*, 190 P.2d 575 (Wash. 1948). If a renunciation has occurred, the community property is reclassified and management rights change accordingly.

In most cases from other community property jurisdictions, however, the courts have been unwilling to find a renunciation of the community even though the parties have lived apart for a significant period. *See Rustad v. Rustad*, 377 P.2d 414 (Wash. 1963). When spouses live separate and apart in Arizona, there is a fixed rule that such separation has no effect on the classification process and thus no effect on management and control, except for assets whose management is determined by possession. *Flowers v. Flowers*, 578 P.2d 1006 (Ariz. Ct. App. 1978); *see also* Reppy & Samuel, *supra* § 4.9, at 289. Other states have statutes dealing with the effect of spouses not living together. *See, e.g.*, Cal. Fam. Code Ann. § 771 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 20 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot).

Because living apart does not change the Act's application, inequities can arise. For example, debts incurred by one spouse in the interest of the marriage or the family can be satisfied through garnishment of the other spouse's wages. One-half of a spouse's savings from his or her earnings are owned by the other spouse. All interspousal remedies still exist.

However, inequities can also arise in the states whose statutory law provides for all property acquired after separation to be separate property. For example, under the California statute, if one spouse is employed and the other is not, and during separation the nonemployed spouse uses savings accumulated during marriage for support (community property) while the employed spouse saves an equal amount of his or her income (separate property), the expended community savings are in effect transformed into separate property. *See* Carol S. Bruch, *The Legal Import of Informal Marital Separations: A Survey of California Law and a Call for Change*, 65 Cal. L. Rev. 1015 (1977). In Wisconsin, management basically follows title and possession. In most instances, living apart will not significantly change the spouses' respective management rights.

## G. Disability or Absence [§ 4.58]

The Act does not expressly address the effect of a spouse's disability or incompetence on management rights. The rights to manage and control property therefore continue in each spouse as if the disability had not occurred. However, under other rules, the incompetent spouse may be unable to exercise management and control powers over property held in his or her name or in his or her possession. In addition, the incompetent spouse may be unable to act together with the other spouse in making gifts in excess of \$1,000 in a calendar year or with regard to marital property assets held in the names of both spouses other than in the alternative. *See* Wis. Stat. §§ 766.51(2), .53.

For these reasons and others, the Act provides that a court may appoint a conservator or guardian to exercise a disabled spouse's rights to manage and control marital property assets. *See* Wis. Stat. § 766.51(7). Once appointed, a guardian of the estate may, with the court's approval, exercise on behalf of the incompetent spouse any management and control right over a marital property asset and any right in the business affairs that the spouse could exercise under chapter 766. Wis. Stat. § 54.20(2)(h). The Act specifically authorizes a guardian or conservator to consent to act together or join in any transaction for which the consent or joinder of both spouses is required and to execute a marital property agreement. *Id.* The guardian or conservator may not, however, make, amend, or revoke the incompetent spouse's will. Wis. Stat. § 54.20(2)(h). It appears that because court approval is required, the other spouse may be the guardian or conservator, even if he or she may have a conflict of interest, and as such may give the required consent for transactions requiring the spouses to act together.

The competent spouse could also proceed under section 766.70(3), the add-a-name remedy, to have his or her name added to any marital property asset (other than certain business interests) held in the other spouse's name. *See infra* § 8.24.

➤ **Comment.** Section 766.70(3) does not expressly prevent the add-a-name remedy from being used to name both spouses in the alternative. If the spouses are named in the alternative, the competent spouse would have the right to solely manage the marital property assets. However, it is not likely that the remedy can be used to name the spouses in the alternative. *See infra* § 8.24.

In addition to using the add-a-name remedy, the competent spouse could proceed under section 766.70(4) to limit or terminate the incompetent spouse's management rights. *See infra* ch. 8 (discussion of the remedies under section 766.70).

When assets are held in both names other than in the alternative, the spouses must act together for purposes of management and control. Wis. Stat. § 766.51(2). If an emergency arises when one spouse is away on a trip or hospitalized in a different community, the issue is whether the present spouse can obtain the temporary right to manage this property without the absent spouse's joinder. There is not a clear answer to this question. Section 54.50 permits the appointment of a temporary guardian, but the statute applies only to situations in which a minor, a spendthrift person, or an alleged incompetent person is involved. The spouses could provide for this possibility by executing a durable power of attorney and indicating that the power should go into effect on signing or on determination of lack of capacity.

Section 766.70(4) allows the court to limit or terminate an absent spouse's management rights. However, the statute does not define what constitutes an absence of sufficient duration to invoke the provision. Because the provision is not in UMPA, UMPA does not provide guidance. If a short absence permits invocation of the remedy, it could facilitate management and in some circumstances prevent breaches of contract. *See infra* § 8.30. However, it appears that a permanent or at least a significant, rather than a temporary, absence may be required before this remedy can be granted, since spousal absence is joined in the statute with gross mismanagement and waste. Gross mismanagement and waste are affirmative conduct against the interest of the marriage by the spouse whose rights are being terminated. A temporary, explained absence is not against the interest of the marriage. If an order under section 766.70(4) is not available, no statutory remedy seems to exist when a spouse is temporarily absent. The cases in the other community property states seem to require that a manager spouse have shirked responsibility before an emergency can be deemed to justify the termination of that spouse's management power. *See McKinney v. Boyle*, 447 F.2d 1091 (9th Cir. 1971); *Wright v. Hay's Adm'r*, 10 Tex. 130 (1853); *Marston v. Rue*, 159 P. 111 (Wash. 1916); *see also* Reppy & Samuel, *supra* § 4.9, at 233.

## H. Guarantees [§ 4.59]

A guarantee may arise either in a transaction that benefits the marriage or the family or in a gratuitous (i.e., nonbeneficial) transaction. *See infra* § 6.22. If the spouses obtain a benefit from the guarantee, such as when a spouse guarantees a loan to a business that employs a spouse, the guarantee in all likelihood is for a family purpose, and if the principal obligor defaults, the obligation then may be satisfied in the same manner as any other family-purpose obligation. Wis. Stat. § 766.55(2)(b). If the guarantee is gratuitous, such as a guarantee of a relative's note, it is unclear whether the obligation is for a family purpose, and thus the extent to which marital property assets are available in the event of default is unclear.

The Act does not contain any express provision dealing with a spouse's authority to guarantee an obligation. However, both spouses seem to have the management and control power to guarantee an obligation, regardless of whether the guarantee is gratuitous. *See* Wis. Stat. § 766.51; *In re Groff*, 131 B.R. 703 (Bankr. E.D. Wis. 1991). It is unclear whether a gratuitous guarantee is subject to the gift limitations in section 766.53 if marital property assets could be reached when the principal obligor defaults. The better view is probably that section 766.53 does not apply. *See supra* § 4.36. This is particularly true if the guarantor has assets classified as individual or predetermination date property that could also be reached to satisfy any claim based on the guarantee.

## I. Transfer to Survivorship Marital Property [§ 4.60]

If a spouse dies while holding marital property assets in his or her name, the surviving spouse owns a one-half interest in the asset and the other one-half interest passes as part of the deceased spouse's estate. The Act also permits marital property assets to be held in a form that provides survivorship ownership. Wis. Stat. § 766.60(4). If the words *survivorship marital property* are used instead of *marital property*, the complete ownership rights vest solely in the surviving spouse by nontestamentary disposition at death. Wis. Stat. § 766.60(5)(a).

Survivorship marital property is an important substantive addition to normal community property concepts made by UMPA and adopted in Wisconsin. *See* UMPA § 11 cmt. It is "not a form of joint tenancy but is

a new statutory estate.” *Id.* As the comment to UMPA section 11 explains, “[i]t is not intended to carry on the arcane doctrines of joint tenancy but simply to establish a nonprobate survivorship incident by the utilization of the appropriate words on a document of title or other medium by which property is held.” The survivorship element is consistent with the policy of Uniform Probate Code section 6.101 and with the ability to create a nontestamentary disposition by marital property agreement. *See* Wis. Stat. § 766.58(3)(f).

The spouses may create survivorship marital property by reregistering an existing asset or by expressing the intent to create survivorship marital property in the document of title at the time of acquisition. *See* Wis. Stat. § 766.60(5). Under section 766.605, if either marital property funds or nonmarital property funds are used to acquire a homestead after the determination date, the homestead is survivorship marital property if both names are on the title, unless a contrary intent is expressed on the instrument of transfer or in a marital property agreement. For example, if a deed for a homestead is in the name of “H and W, husband and wife,” after the determination date, the homestead is survivorship marital property regardless of the classification of the funds used for the acquisition or the spouses’ intent (unless reflected in the deed). Wis. Stat. § 766.605.

➤ **Note.** The above rule applies only if the homestead is held between both spouses when the asset is acquired. Thus, if the homestead is initially held in the name of one spouse and is subsequently transferred into the names of both spouses, section 766.605 will not apply, and, if survivorship is intended, the document of title must so indicate.

A relevant issue concerns whether one spouse who holds a marital property asset may, acting alone, transfer the marital property asset into the survivorship marital property form of holding. There is no express provision that management and control powers either may or may not be used by one spouse acting alone to create survivorship marital property. If one spouse acting alone can transform a marital property asset into survivorship marital property, it deprives the first spouse to die of the right to dispose of one-half of the asset by will or intestate succession to some other person. For example, in a second marriage in which the wills of both spouses give property to children from prior marriages, such a change in form of holding would disinherit the children of the first spouse to die as to any asset so held.

The plural *spouses* in the section 766.60(4) survivorship provisions is also used in the other provisions of the statute that describe forms of holding marital property assets in both names. *See* Wis. Stat. § 766.60(1), (2). It is unlikely that the use of the plural “spouses” in each of these subsections means that joinder is required. Thus, absent an express limitation, a spouse acting alone may probably use his or her management and control powers to create survivorship marital property. The transaction is subject to review to determine if it satisfies the spouse’s duty of good faith. *See* Wis. Stat. § 766.15(1).

If property is held as survivorship marital property, another issue concerns whether one spouse may sell the asset and convert the proceeds to marital property without survivorship. One spouse acting alone may can manage and control the asset if it is held in the name of both spouses in the alternative. Wis. Stat. § 766.51(1)(b). Section 766.60(5) appears to require the precise term *survivorship marital property* on the title for all assets held in that form. Two exceptions are that a homestead is survivorship marital property when section 766.605 applies, and attempts by spouses to create joint tenancies after the determination date instead create survivorship marital property. Wis. Stat. § 766.60(4)(b)1. Thus, when a survivorship marital property asset is sold, the proceeds do not seem to be survivorship marital property unless so stated on the check. If one spouse acting alone has management and control rights over an asset held as survivorship marital property, that spouse appears able to change the form of holding to one without survivorship. Wis. Stat. § 766.60(4)(b) Legis. Council Note—1985 Act 37, §§ 124 to 126 (West 2009). This change in holding is also subject to the other spouse’s remedies for failure to comply with the obligation of good faith.

## **J. Transfer of Marital Property in Trust [§ 4.61]**

If a spouse has management and control rights with regard to a marital property asset, may that spouse use that power to transfer the marital property asset to a trust? If so, the asset’s management and control is subsequently determined by the terms of the trust. Wis. Stat. § 766.51(3).

A trustee may administer, manage, and distribute the trust property in accordance with the terms of the governing instrument regardless of the classification of the property in the trustee’s possession unless the trustee has received a written notice of claim in a court order or in the terms of a

trust. Wis. Stat. § 766.575(2). Thus, after the death of a spouse, the trustee may continue to administer the assets pursuant to the trust provisions even though some of the assets may be classified as marital property that will be distributed as part of the decedent's estate.

Under the Act, a spouse may use management and control rights to transfer marital property assets to a revocable trust. *See infra* ch. 10. Section 766.31(5) provides that the transfer of marital property assets to a trust does not by itself change the property's classification. The statute is based on UMPA section 4, the comment to which states that it was designed "to permit the creation of revocable living trusts by one or both spouses without any automatic reclassification of property committed to the trust." Thus, if a marital property asset is transferred to a revocable inter vivos trust, the property retains its classification as marital property, and one-half of the asset is subject to testamentary disposition by each spouse. The transfer is subject to the spouse's obligation of good faith.

It is unclear whether the nondonor spouse can withdraw the marital property assets from the trust during his or her lifetime. If the marital property asset was held solely by the donor spouse, the nondonor spouse probably lacks such power, since the nondonor spouse never had management and control rights regarding the asset. The add-a-name remedy is not available after the asset is transferred to the trust. Wis. Stat. § 766.70(3) (asset titled in trust, not in spouse). If the asset was held in both names in the alternative or was not held, the asset was subject to the nondonor spouse's management and control before its transfer to the trust. It appears, however, that the transfer terminates the nondonor spouse's management and control power, because the terms of the trust determine the right to manage and control a marital property asset transferred to a trust. *See* Wis. Stat. § 766.51(3). This is consistent with general trust law, under which the trustee has legal title. George G. Bogert, *The Law of Trusts and Trustees* §§ 141 (3d ed. 2007), 611 (3d ed. 2003). Thus, if the nondonor spouse no longer has management and control rights, it is likely that he or she cannot remove a marital property asset from the trust.

After the death of the nondonor spouse, it appears that the trustee can continue to manage and control the trust's assets under the terms of the trust. The trustee is not obligated to determine the classification of the trust assets or required automatically to transfer one half of all assets classified as marital property to the nondonor spouse's estate. However, the personal representative of the nondonor spouse's estate can reach the



nondonor spouse's share of the marital property assets. *See infra* ch. 12. If the trust instrument appoints the donor spouse as trustee or otherwise permits the donor spouse to direct distributions to third parties, such power may be exercised by that spouse. The exercise of this power would end the assets' classification as marital property and the transfer would be subject to the limitations on the amount of gifts of marital property assets and the obligation of good faith. *See supra* ch. 2, *infra* ch. 10.

If a marital property asset is transferred to an irrevocable trust, the issue is whether the property retains its classification as marital property or whether other factors indicate an intention to make a gift. *See* Wis. Stat. § 766.31(5); *see also supra* § 4.36. The comment to UMPA section 4 does not discuss a transfer to an irrevocable trust. Whether a gift was made can be decided on the facts of each case. If there was no gift, the asset remains marital property, and management and control rules for marital property transferred to a revocable trust should apply.

➤ **Note.** The classification of assets in a trust can have tax implications. In Private Letter Ruling 199908032 (Nov. 30, 1988), the Internal Revenue Service approved the transfer as a one-half interest in a community property residence to each of two identical personal residence trusts as provided for in I.R.C. § 2702(a)(3)(A)(ii). Each trust was to terminate on the termination date, which was the earlier of: (1) the date 15 years after the date of the trust agreement, and (2) the date of the trustor's death. The trustor was the sole beneficiary during the initial trust term. Did the transfer change the classification by gift? If not, do both spouses have a one-half interest in the trust created by the other spouse and, at death, does the surviving spouse have a right to withdraw one half of the trust assets? These issues were not considered in the ruling. To obtain the tax advantages of a personal residence trust it is necessary that the residence no longer be classified as marital property.

## **K. Change of Domicile to Another Jurisdiction [§ 4.62]**

If spouses move to another jurisdiction, the marital property assets they acquired while domiciled in Wisconsin generally retain their classification in the new jurisdiction. *See infra* § 13.19. The property remains marital property as long as it can be traced to marital property

assets acquired while the spouses were married and domiciled in Wisconsin.

What management and control rights exist as to such property after the change of domicile? Logically, the management and control rights applicable while the spouses were Wisconsin residents should remain applicable to the marital property assets in the new jurisdiction because these rights arguably are an incident of marital property classification. This should be the result under the conflict-of-laws principles discussed in chapter 13, *infra*. However, courts in the new domicile may not always recognize these rights.

Under section 766.03(3), a change of domicile to a new jurisdiction by one or both spouses does not affect the property available to satisfy any obligation incurred by a spouse while both spouses are domiciled in Wisconsin. Similarly, under section 766.03(6), the property available to satisfy an obligation incurred by a spouse while one or both spouses are not domiciled in Wisconsin is not affected by chapter 766. Wis. Stat. § 766.03(6).

➤ **Comment.** Whether these statutes will achieve the legislative objectives will depend on the willingness of the courts in other states to use these provisions. *See infra* §§ 6.45, 13.19.

## IV. Bona Fide Purchaser [§ 4.63]

### A. Definition and Statutory Protection [§ 4.64]

The effectiveness of the Act's management and control provisions is determined to a large extent by the ease with which a third party can become a bona fide purchaser. A *bona fide purchaser* is defined as "a purchaser of property for value who was not knowingly a party to fraud or illegality affecting the interest of the spouses or other parties to the transaction, does not have notice of an adverse claim by a spouse and acted in the transaction in good faith." Wis. Stat. § 766.57(1)(a). The word *purchase* is broadly defined to mean "to acquire property by sale, lease, discount, negotiation, mortgage, pledge or lien, or otherwise to deal with property in a voluntary transaction other than a gift." Wis. Stat. § 766.57(1)(b). Because the Act does not define the word *gift*, existing Wisconsin law must be used for the definition. *See, e.g., Geise*

*v. Reist (In re Estate of Reist)*, 91 Wis. 2d 209, 281 N.W.2d 86 (1979); *Wierman v. Wierman*, 130 Wis. 2d 425, 387 N.W.2d 744 (1986).

As a bona fide purchaser, a party is protected from subsequent disputes between the spouses. Section 766.57(3) provides:

[m]arital property purchased by a bona fide purchaser from a spouse having the right to manage and control the property under s. 766.51 is acquired free of any claim of the other spouse and of any claim asserted through or under the other spouse. The effect of this subsection may not be varied by a marital property agreement.

The statute is designed to protect any third party who acquires property in a nondonative transaction. A secured lender is also protected. *See infra* § 5.28. Section 766.57(1)(c) states that “[a] purchaser gives ‘value’ for property acquired in return for a binding commitment to extend credit, as security for or in total or partial satisfaction of a preexisting claim.” A security interest is an interest in property, and its acquisition confers bona fide purchaser status. It is unclear whether an unsecured lender is a bona fide purchaser. *See infra* § 5.28. If the transaction is not a gift, the Act protects the bona fide purchaser even if the managing spouse’s disposition violated the spouse’s obligation of good faith.

## **B. Effect of Marital Property Agreement [§ 4.65]**

When is a purchaser deemed to have notice of a marital property agreement such that the purchaser is subject to the agreement’s terms, and, as a result, may not become a “bona fide” purchaser? The Act defines when a person has notice: “A person has ‘notice’ of a fact if the person has knowledge of it, receives a notification of it, or has reason to know that it exists from the facts and circumstances known to the person.” Wis. Stat. § 766.01(13). However, the Act provides that notice of the existence of a marital property agreement, a marriage, or the termination of a marriage does not affect the status of a purchaser as a bona fide purchaser. Wis. Stat. § 766.57(2). Knowledge of the existence of an agreement does not create an obligation to request a copy and review its provisions. Knowledge of the provisions is necessary, however. A marital property agreement may be recorded with the register of deeds, but the recording does not constitute notice to a purchaser. *See* Wis. Stat. §§ 59.43(1)(r), 766.58(11), .57(2). If the

agreement contains a legal description of real property, is recorded in the county where the real estate is located, and becomes part of the property's chain of title, a third party receiving a conveyance of the real estate appears to have actual notice of the agreement and its provisions and therefore is subject to any terms relevant to the transaction. *See* Wis. Stat. § 706.09; *see infra* § 4.73. The same result would apply to a recorded writ of attachment or *lis pendens*. *See* Wis. Stat. § 59.43(1)(a).

➤ **Query.** What occurs if the marital property agreement classifies all property of the spouses as nonmarital property? By its terms, section 766.57(3) only protects a bona fide purchaser who purchases *marital property assets* from a spouse. If the spouses by agreement do not have any marital property assets, does this mean the statute does not apply to a sale by either spouse of an asset to a third party? That is clearly one possible interpretation, and it would be necessary to look to other law to determine if the purchaser qualified as a bona fide purchaser. The other possible interpretation is that the property classification in the marital property agreement varies the effect of section 766.57(3) and thus is inoperative against the bona fide purchaser as to any property that would have been marital property but for the agreement. *See* Wis. Stat. § 766.57(3) (“The effect of this subsection may not be varied by a marital property agreement.”) The statutory provision comes from UMPA section 9(c), but the comment to that section does not indicate which analysis is correct. If the marital property agreement is inoperative, the purchaser is in a better position than a creditor, since knowledge by a purchaser of the existence of a marital property agreement does not constitute notice. The purpose of section 766.57(3) is to protect a purchaser dealing with a spouse, and the statute should be construed to provide that protection.

### C. Notice of Adverse Claim [§ 4.66]

Under the Act, a purchaser with notice of a spouse's adverse claim is not protected as a bona fide purchaser. *See* Wis. Stat. § 766.57(1)(a). The key question concerns when a purchaser has notice of an adverse claim by a spouse. *See* Richard V. Wellman, *Third Party Interests Under the Uniform Marital Property Act*, 21 Hous. L. Rev. 717, 725–26 (1984). Except for recording documents in the chain of title for Wisconsin real estate, a spouse can generally do little to ensure that a third party has actual notice of an adverse claim. Knowledge of the

existence of a marital property agreement is not actual notice of an adverse claim. Wis. Stat. § 766.57(2). However, a purchaser of real estate should be considered to have actual notice of an adverse claim to a parcel of real estate if the claim has been recorded as part of the chain of title; a third party cannot acquire a parcel of real estate and expect it to be free of claims without checking the title. If a marital property agreement were recorded in the chain of title, the purchaser should be required to inquire about the terms of the agreement. *See infra* § 5.134.

If a court has entered an order restricting a spouse's management of an item of marital property that is not real estate, the burden should be on the spouse desiring protection either to have the restrictions indicated on the title to the asset or to have the title transferred out of the name of the spouse who has been deprived of management authority. It would be unduly burdensome if purchasers were required to check all Wisconsin court records to determine whether a spouse holding property has been deprived of present authority to manage it.

For this same reason, if a spouse has commenced an action to limit the other spouse's management powers, a third party should not have the burden of inquiring about the litigation or attempting to ascertain independently whether litigation exists. Nor should a court determination terminating the marriage or limiting one spouse's management powers have greater status than that afforded to marital property agreements, unless the marital property asset is real estate and the determination is recorded in the chain of title.

The Act protects a bona fide purchaser in transactions occurring after termination of the marriage, even though an order of dissolution or an order in the probate proceedings may have reclassified assets or restricted management of those assets. *See* Wis. Stat. § 766.57(2). A former spouse's sale of property held in his or her sole name, or of untitled property in his or her possession, should not be voidable. *See id.* In summary, the effect of section 766.57 is that actual notice of an adverse claim is necessary to prevent a purchaser from attaining bona fide purchaser status.

### **D. Bona Fide Purchaser Status Requires Purchaser to Determine Spouses' Management and Control Rights [§ 4.67]**

One uncertainty for purchasers arises from the definition of the word “held.” Wellman, *supra* § 4.66, at 732. To determine which spouse has management and control powers under the Act, a purchaser must be able to determine whether a marital property asset is held. In addition to certain account relationships, documents of title, uncertificated securities and general partnership interests, the definition of the word held also recognizes a writing that “customarily operates as a document of title to the type of property” involved and that is issued in the person’s name. *See* Wis. Stat. § 766.01(9)(a). Under this definition, it is unlikely that a bill of sale for household tangible personal property or a receipt for the purchase price paid for tangible personal property qualifies as a writing in the person’s name that customarily operates as a document of title to the type of property; therefore, this property would not be held by a spouse. *See supra* § 4.5; *see also* Wellman, *supra* § 4.66, at 732–35. Accordingly, not every document can be accepted by a purchaser as proof of management and control rights under section 766.51. Likewise, bona fide purchaser status should not be subsequently threatened as a result of casual documents that the purchaser may or may not actually know are in existence.

When property is held in the name of both spouses other than in the alternative, a purchaser who does not obtain both spouses’ signatures probably is acting at his or her peril since the rules for management and control for such property require that the spouses act together. *See* Wis. Stat. § 766.51(2). Thus, if the purchaser obtains only one signature, the purchaser will not become a bona fide purchaser.

If an asset is held in the names of both spouses in the alternative, the purchaser may want to request both spouses’ signatures unless the property’s classification as marital property is clear. If the asset is marital property, only one signature is required. *See* Wis. Stat. § 766.51(1)(b). However, the signature of both spouses is required to convey the entire interest if the asset is individual property or predetermination date property, or if it is mixed property having a marital property component, or if it is held by the spouses in co-ownership, as tenants in common, or in joint tenancy.

### **E. Spouses' Right to Commence Action for Breach of Contract Against Purchase [§ 4.68]**

The Act expands a purchaser's liability in one way that did not exist under the common law. When there is a breach of a contract involving a marital property asset, each spouse acting alone may have the right to commence an action to protect the spouses' interest in the marital property asset, rather than only the spouse who was a party to the contract. *See supra* § 4.52. However, when an action is commenced by only one spouse, that spouse can bind both spouses' interests in the marital property asset, and the other spouse can be joined as a party. Wis. Stat. § 803.04. In addition, while the chance of a suit is expanded, the exposure is not increased. Thus, this change does not appear to significantly expand the purchaser's risk. *See Wellman, supra* § 4.66, at 735.

### **F. Summary [§ 4.69]**

The Act is intended to permit third persons to enter into transactions involving marital property assets with one spouse without concern for the other spouse's rights if the participating spouse holds the marital property asset, has a right under or contract to deal with the asset or claim, or has apparent management of the marital property asset through possession. A marital property agreement may change the statutory management and control provisions, Wis. Stat. § 766.58(3)(b), but the agreement cannot prevent a third party who purchases from a spouse with management rights under section 766.51 from becoming a bona fide purchaser and therefore cannot expand the purchaser's risk. Wis. Stat. § 766.57(3). If a marital property asset has been reclassified by judicial determination but the title has not been changed in accordance with the order, the third party may reasonably deal with the spouse in whose name the asset is held. Actual knowledge of the existence of an agreement or court order does not constitute actual notice to affect a purchaser's attaining the status of bona fide purchaser. Notice that eliminates bona fide purchase status exists only if the purchaser actually knows or should have known the terms of the agreement or court order at the time of purchase.

## V. Management of Real Estate [§ 4.70]

### A. In General [§ 4.71]

Sections 4.72–.74, *infra*, describe the Act’s management rules to the management of real estate. The discussion relies on and refers back to the chapter’s more detailed analysis of the rules in previous sections. Sections 4.72 and 4.73, *infra*, discuss management and control of real estate at the time of and after acquisition, respectively. Section 4.74, *infra*, offers two examples that apply the rules to specific facts.

➤ **Note.** The discussion in sections 4.72–.74, *infra*, assumes that all or part of the real estate is classified as marital property. The right to manage and control individual or predetermination date property is exclusively in the owner spouse or spouses, *see* Wis. Stat. § 766.51(1)(a), and is not discussed here.

### B. Management and Control at Acquisition [§ 4.72]

Under the Act, either spouse acting alone, or both spouses acting together, may purchase real estate that will be classified as marital property. The right to manage the real estate is distinct from its classification and does not determine its classification. Wis. Stat. § 766.51(5). In general, classification is determined by the source of the funds used for the asset’s acquisition, whereas management and control rights are determined by how the asset is held. The concept of holding is discussed in section 4.5, *supra*, and generally depends on how the asset is titled. Consideration of how an asset is held is relevant only for assets classified at least in part as marital property. *See* Wis. Stat. § 766.51(1)(am), (b).

As mentioned above, the initial classification of the real estate generally depends on the classification of the funds or property used for its acquisition. If an asset is acquired during marriage through incurring debt, the portion of the asset attributable to the debt proceeds may well be classified as marital property. *See supra* § 3.33. If more than one classification of funds is used, a mixed asset is created involving pro rata ownership interests. *See supra* § 3.32.



In other cases, the statute specifies classification or form of holding, without regard to the source of funds used. For example, a homestead acquired in both names exclusively between spouses after the determination date is held as survivorship marital property if no intent to the contrary is expressed on the instrument of transfer or marital property agreement. Wis. Stat. § 766.605. Thus, if the spouses prefer to have both names on the title but do not wish to hold their homestead as survivorship marital property, the acquiring spouse could specify a contrary intent in the contract to purchase or execute a marital property agreement. The intention also must be reflected on the document of transfer (normally, the deed of conveyance). The Act also appears to permit a different form of holding for a homestead to be accomplished by other means, such as by a gift. Wis. Stat. § 766.31(10). Management and control exercised in the contract to purchase includes the right to determine how an asset will be held.

After the determination date, the Act also governs attempts by spouses to create a tenancy in common or a joint tenancy. An attempt to create a tenancy in common instead creates marital property, and an attempt to create a joint tenancy instead creates survivorship marital property. Wis. Stat. § 766.60(4)(b). Under the common law, both tenants in common or both joint tenants must join in managing the asset or in conveying the entire asset. Acting alone, one tenant can only manage his or her one-half interest in the asset. Under the Act, if the form of holding is in the alternative (i.e., “or”), either spouse acting alone may manage the entire asset. After the determination date, a joint tenancy or tenancy in common exclusively between spouses may be created only under the express provisions of a marital property agreement. The same rule applies to property gifted to both spouses by a third party. The asset is classified marital property or survivorship marital property unless the donor provides otherwise.

If the acquired real estate will be classified as marital property, the real estate is not “held” until the closing occurs and title is received. Management rights based on how the real estate is held can only be analyzed after the ownership interest is acquired; before receipt of title, there is only a contract to purchase the property, and the contract is not held by either spouse. *See supra* § 4.5. Although an equitable conversion may have occurred, the purchase contract does not make the real estate held by the acquiring spouse. *See* Wis. Stat. § 766.01(9). The purchase contract determines how title will be received, and this

provision at least initially determines the management and control of the real estate after the closing.

The contracting spouse acting alone may incur purchase-money indebtedness in connection with the acquisition of the property. *See* Wis. Stat. § 766.51(1m). The contracting spouse acting alone may create a security interest in the property being acquired. *See* Wis. Stat. § 766.51(1m). After the property is acquired, a security interest or mortgage can only be created by a spouse having the right to manage and control the asset. *See* Wis. Stat. § 766.51(1m)(b).

A purchase contract that designates how the asset is to be held after acquisition affects the property's subsequent management and control. If both spouses' names are on the title to the property, the Act expressly authorizes that those names be listed either in the conjunctive or in the alternative (i.e., "and" or "or"). *See* Wis. Stat. § 766.51(1)(b), (2). The use of the alternative ("or") is only permissible if the asset is entirely marital property. If the asset is marital property and both names are listed in the conjunctive ("and"), both spouses must act together in managing the property. Wis. Stat. § 766.51(2); *see supra* §§ 4.44–.48. If a portion is not classified as marital property (i.e., is individual or predetermination date property in joint tenancy or tenancy in common), the form of holding should be in the conjunctive ("and") to reflect the management rules applicable to such co-tenancies.

➤ **Comment.** If the asset is initially acquired using debt proceeds, is classified as marital property, and is held in both names in the alternative, a classification question occurs if the debt obligation is satisfied using nonmarital funds. In this situation, part of the ownership interest probably becomes nonmarital property. *See supra* § 3.41. As a result, because part of the ownership interest is nonmarital property, neither spouse can manage the entire asset acting alone, and thus the management rules applicable to the alternative form of holding are no longer believed effective.

A marital property agreement can specify how an asset is held and the management of specific assets. The Act authorizes spouses to enter into marital property agreements and to vary the Act's provisions by those agreements. Wis. Stat. § 766.58. A marital property agreement can affect the rights in and obligations with respect to any property, as well as the management and control of any property. Wis. Stat. § 766.58(3)(a), (b). Thus, spouses can classify presently owned or

subsequently acquired real property in any manner they desire by a specific agreement relating to that asset or by a general agreement classifying most or all of their assets. Likewise, they can specify each spouse's management and control rights in any or all of their property. A marital property agreement is binding between the spouses if it complies with the statutory requirements. *See infra* ch. 7. The agreement provisions are binding on a creditor only if the creditor has actual knowledge of the provisions before extending credit. Wis. Stat. § 766.55(4m). The agreement affects third-party bona fide purchasers only if the purchaser has notice at the time of purchase of an adverse claim by the other spouse arising under the agreement because of the transaction. *See* Wis. Stat. § 766.57; *see also supra* § 4.66.

### **C. Management and Control After Acquisition [§ 4.73]**

Under the Act, either spouse acting alone may manage and control that spouse's property that is not marital property and all marital property held in that spouse's name alone. Wis. Stat. § 766.51(1)(a), (am). If the real estate is classified as marital property and is held in one spouse's name, the spouse in whose name the property is held has exclusive management and control rights. Wis. Stat. § 766.51(1)(am). If the real estate is classified as marital property and the nonholding spouse wishes to obtain management and control rights without the holding spouse's consent, the nonholding spouse may initiate an action to have his or her name added to the document that evidences ownership. *See* Wis. Stat. § 766.70(3). This remedy is not available if the real estate is part of a sole proprietorship business operation and the nonholding spouse is not involved in operating or managing the business. Wis. Stat. § 766.70(3)(c).

A spouse exercising management and control powers over marital property assets has an obligation to exercise these powers in good faith. Wis. Stat. § 766.15(1). If a spouse exercises management rights by making a gift of marital property real estate to a third party, the nondonor spouse may have a remedy to recover the asset or obtain a compensatory judgment. Wis. Stat. §§ 766.53, .70(6)(b); *see infra* § 8.45. However, if there is a purchase instead of a gift, under section 766.57(3) a third party will become a bona fide purchaser if the third party acquires marital property real estate for value from a spouse having management and control of the property under the Act. That third party acquires the property free of any claim of the other spouse and free of any claim

asserted through or under the other spouse. Wis. Stat. § 766.57(3). Section 766.57(3) may not be varied by a marital property agreement. *See supra* §§ 4.63.–.69.

The general rules are summarized as follows:

<b>Ownership or Classification of Property</b>	<b>Forms of Holding</b>	<b>Management and Control</b>
I. Individual Property	Sole name of one spouse	Exclusive with owner (Wis. Stat. § 766.51(1)(a))
	By marital property agreement —tenancy in common and joint tenancy with spouse	Both spouses together for whole asset; each alone for his or her interest
	Tenancy in common or joint tenancy with third party	Both parties together for whole asset; each alone for his or her interest
	Trust	Trustee, under trust provisions (Wis. Stat. § 766.51(3))
	Not titled, such as lease interest of less than one year, adverse possession claim, or prescription right	Exclusive with owner (Wis. Stat. § 766.51(1)(a))
II. Marital Property	Sole name of one spouse	Exclusive with holding spouse (Wis. Stat. § 766.51(1)(am))
	Names of both spouses Alternative (i.e., “H or W”) Conjunctive (i.e., “H and W”)	Either spouse acting alone (Wis. Stat. § 766.51(1)(b)) Both spouses must act together (Wis. Stat. § 766.51(2))
	Survivorship marital property (i.e., “H and W, as survivorship marital property”)	Determined by whether holding in conjunctive or alternative
	Trust	Trustee, under trust provisions (Wis. Stat. § 766.51(3))

Ownership or Classification of Property	Forms of Holding	Management and Control
	Not held, such as lease interest of less than one year, adverse possession claim, or prescription right	Either spouse acting alone (Wis. Stat. § 766.51(1)(am))
III. Predetermination Date	Same as individual property, except joint tenancy and tenancy in common between spouses can exist without marital property agreement	Rules same as for individual property (Wis. Stat. § 766.51(6))
IV. Mixed Property	Any form of holding for categories I-III	Same rules for each component, as set forth in categories I-III

The Act requires that the spouses act together in managing marital property real estate held in the names of both spouses in the conjunctive. Wis. Stat. § 766.51(2); *see also* Wis. Stat. § 766.53 (gifts to third parties). It appears unlikely that the requirement that spouses act together has the same meaning in sections 766.51(2) (management and control of marital property) and 766.53 (gifts of marital property to third persons). *See supra* §§ 4.35–.42, .44–.48. The requirement probably necessitates that both spouses join in any conveyance of real estate. It is unlikely that one spouse can sign a conveyance on one date and the other spouse can later consent to the transaction and have that consent be sufficient to create a valid transfer as of the date the first spouse signed. *See supra* §§ 4.35–.42, .44–.48. Because the form of holding is known through the chain of title, a third party would have actual notice and would know he or she was not receiving a conveyance from all parties required to exercise management and control rights under the Act. Thus, the purchaser would not become a bona fide purchaser at the initial date of the transaction. Therefore, all intervening transactions involving the real estate and placed on record would have precedence.

What is required for an effective contract to repair, maintain, or remodel marital property real estate? It is unlikely that the rule that spouses must act together in the management and control of marital property assets held in the conjunctive form (“and”) requires that both spouses affirmatively participate in management transactions other than conveyances and leases for more than one year. In other community

property states where joinder is required for managing real estate, this requirement has not been extended to contracting for routine services to repair or maintain the real property. *See supra* § 4.46. It is likely that this conclusion will be adopted in Wisconsin.

If both spouses must act together and one spouse becomes incompetent, a guardian can be appointed for that spouse so that both spouses can act together in managing the property. *See* Wis. Stat. § 54.20(2)(h). While management by a guardian is subject to court approval, it appears that the other spouse may be appointed as the guardian even though a conflict of interest may arise. *Id.* Subsequent management and control could also be authorized by the spouses through a durable power of attorney. *See* Wis. Stat. ch. 244 (created by 2009 Wis. Act 319).

A third party becomes a bona fide purchaser if he or she purchases the real estate for value, is not knowingly a party to fraud or illegality affecting the spouses' interests, does not have notice of an adverse claim by a spouse, and acts in the transaction in good faith. Wis. Stat. § 766.57(1); *see supra* §§ 4.63–.69. Notice of the existence of a marital property agreement, a marriage, or the termination of a marriage does not affect a purchaser's status as a bona fide purchaser. Wis. Stat. § 766.57(2). It appears, however, that if a marital property agreement is recorded with the register of deeds and becomes a part of the chain of title to the real estate, then any provisions in that agreement changing the real estate's classification or changing the related management and control rights are binding on the third party. Wis. Stat. § 706.09. If a marital property agreement is recorded in the chain of title, the third party has notice of any change by the agreement of the basic statutory management and control rights. If the recording is not in the chain of title or there has been no recording, it appears that the purchaser would become a bona fide purchaser only if the purchaser dealt with the spouse having management and control powers under section 766.51.

➤ **Comment.** It is believed that if the third party obtains a copy of the agreement, whether through its being in the chain of title or otherwise, the third party must read the agreement and follow its provisions or otherwise act at his or her peril. This is required regarding other documents in the chain of title.

The power of management and control includes the power to change how the asset is held, based on the holding spouse's authority to transfer,

exchange, or dispose of the asset. *See* Wis. Stat. § 766.01(11). Thus, if initially real estate is held exclusively in the name of one spouse, that spouse may change the form of holding to the names of both spouses. This may or may not include a change in classification, depending on the holding spouse's intent. Likewise, a spouse holding marital property real estate in both names in the alternative may change that form of holding to survivorship marital property. A spouse holding real estate in the alternative as survivorship marital property may change the form of holding to marital property without the survivorship incident. *See supra* § 4.60. A spouse having the right of management and control of marital property real estate may also transfer the property to a trust. *See supra* § 4.61. The transfer of the real estate to the trust by itself does not change the property's classification. Wis. Stat. § 766.31(5). Thus, if real estate classified as marital property is transferred to a revocable trust, it is likely that the asset remains classified as marital property. Management and control rights, however, pass to the trustee following the transfer. Wis. Stat. § 766.51(3). If the real estate classified as marital property is transferred to an irrevocable trust for the benefit of a third person, additional facts are present that probably indicate a gift of the property, ending its classification as marital property.

#### **D. Examples [§ 4.74]**

➤ **Example 1.** A husband wants to purchase a parcel of rental real estate. Bank X will loan 80% of the purchase price. The loan is expected to be repaid from cash flow generated by the property. The title is to be held by the husband alone.

1. The husband acting alone may:
  - a. Negotiate terms of purchase and sign the offer to purchase;
  - b. Direct in the offer to purchase how title is held;
  - c. Incur purchase money indebtedness, *see* Wis. Stat. § 766.51(1m);
  - d. Negotiate the lease of the property;
  - e. Contract for maintenance of the property;
  - f. Contract for capital improvements to the property;
  - g. Mortgage the property as security for new or existing indebtedness;
  - h. Commence an action regarding the property, *see supra* §§ 4.50–.53;

- i. Defend an action regarding the property, *see supra* §§ 4.50–.53
  - j. Determine when and at what price to sell the property and sign a listing contract with a broker;
  - k. Accept an offer to purchase and thereby contract to sell the property; and
  - l. Execute a conveyance of the property.
2. The husband's actions in each case are subject to the obligation of good faith in section 766.15.
3. Because of the debt financing, at least 80% of the real estate is likely to be classified as marital property. Classification of the interest attributable to the 20% down payment depends on the source of the funds.
4. The wife has no management and control rights under the Act. As to the marital property component, the wife obtains management and control rights under the Act only through a remedy, *see* Wis. Stat. § 766.70(3), (4).

Although the Act grants management and control to the holding spouse, the nonholding spouse may exercise some management and control activities. For example, it is believed that the wife can exercise at least some management and control rights relating to the property's maintenance. *See supra* § 4.46. The wife should be able to contract for fire insurance to protect her interest in the building. Likewise, she should be able to contract for maintenance that if not done could result in damage to the property, such as repair of a leaking roof or malfunctioning furnace. If the roof or furnace cannot be repaired, the wife should have the management authority to contract for a new furnace or roof to protect her interest in the building. If this conclusion regarding the wife's management authority is correct, the wife can contract for maintenance and capital improvements even though a lien against the property could be created by nonpayment for the services or improvement. The permitted exercise of management and control regarding the property is to protect the wife's ownership interest and does not otherwise infringe on the husband's exclusive management and control rights.



➤ **Query 1.** What if the capital improvement or maintenance is not necessary to protect the wife's interest in the property but rather is discretionary and intended to improve the property's value (for example, an addition to the building)? It is inappropriate to require the third-party contractor to determine how the property is held and then to determine whether the improvement is discretionary or the maintenance is necessary. Thus, the contract should be enforceable. However, is this contract by the wife a breach of the duty of good faith or subject to some other remedy by the husband? It is believed that a contract by the wife for a discretionary capital improvement or maintenance would breach her duty of good faith. Operational management and discretionary capital improvements can only be properly exercised by the holding spouse, and remedies exist if the wife wishes to participate in such management.

➤ **Query 2.** If the rent is not paid, may the wife bring an action to recover the rent? In general, an action for damage to a marital property asset may only be maintained by the spouse or spouses who hold the asset, while an action for loss of earned income can be maintained by either spouse. *See supra* §§ 4.50–53. It is believed the right to payment for the use of rental property is an incident of the property, and thus, W acting alone may not commence the action.

➤ **Example 2.** The husband and wife want to purchase a parcel of rental real estate. Bank X will loan 80% of the purchase price. The loan is expected to be repaid from cash flow generated by the property. The title is to be held by the husband and wife as survivorship marital property.

1. The husband or the wife acting alone or both acting together may:
  - a. Negotiate the terms of the purchase and sign the offer to purchase;
  - b. Direct in the offer to purchase how the title is held; and
  - c. Incur purchase-money indebtedness, *see* Wis. Stat. § 766.51(1m).
2. The husband or the wife acting alone may:
  - a. Lease the property for one year or less, *see supra* § 4.46;
  - b. Contract for maintenance of the property, *see supra* § 4.46; and
  - c. Contract for capital improvements to the property. *See supra* § 4.46.

3. The husband and the wife must act together to:
  - a. Exercise management and control rights under the Act, Wis. Stat. § 766.51(2); *see supra* §§ 4.44–.48;
  - b. Mortgage the property as security for new or existing indebtedness, *see supra* §§ 4.44–.48;
  - c. Lease the property for more than one year, *see supra* § 4.46;
  - d. Commence an action regarding the property, *see supra* §§ 4.50–.53;
  - e. Determine when and at what price to sell the property and sign a listing contract with a broker;
  - f. Accept an offer to purchase and thereby contract to sell the property; and
  - g. Execute a conveyance of the property.
4. The husband's and the wife's actions in each case are subject to the section 766.15 obligation of good faith.

## **VI. Management of a Business [§ 4.75]**

### **A. General Rules [§ 4.76]**

If marital property funds are invested in a business organized as a corporation or a partnership, any stock of the corporation or partnership interest received is classified as marital property. *See supra* ch. 2. The investment of marital property funds or property does not cause the underlying assets of the corporation or partnership to be classified as marital property. *See supra* § 3.47; *see also* Wis. Stat. § 178.21 (partnerships). The corporation or partnership owns the business assets and has all management rights with regard to those assets.

The rules regarding management of a business interest that is marital property do not differ in any significant respects from those applicable to all other marital property assets. For example, a spouse's right to manage stock in a corporation depends on how the stock is held. *See* Wis. Stat. § 766.01(9) (defining held).

A spouse holding an interest in a partnership or corporation can use his or her management right to purchase the marital property interest in the business of the nonholding spouse from the estate of the nonholding spouse and thereby retain full control over the business interest. Specifically, section 857.015 permits a spouse holding an interest in a

business other than a sole proprietorship to direct a purchase of the nonholding spouse's marital property interest in the business. The directive may be made by will or other signed writing. If the holding spouse is the surviving spouse, the directive must be issued within 90 days after the nonholding spouse's death. *See* Wis. Stat. § 857.015.

The management and control rules governing the assets of an unincorporated business differ from those governing business assets owned by a corporation or partnership. Because the assets of an unincorporated business are not owned by a business entity, they are subject to normal management and control rights under the Act, with the exception that a nonmanaging spouse may not use the add-a-name remedy, *see* Wis. Stat. § 766.70(3). The use of business interests to obtain credit is discussed in chapter 5, *infra*. Thus, the classification of each asset owned by an unincorporated business must be determined. If the asset is individual or predetermination date property, management and control rests with the owner spouse or spouses. Wis. Stat. § 766.51(1)(a).

If the asset of the unincorporated business is marital property, it is necessary to determine whether the asset is held by a spouse within the meaning of section 766.01(9). Many such assets, such as real estate, securities, and bank accounts, are held by a spouse. For example, if the bank account for the business is in one spouse's name, that spouse has the sole right to manage that business asset under the Act's general management and control provisions. Likewise, if the business inventory consists of titled assets, such as automobiles, title determines which spouse has the right to manage an asset.

Management and control rights as to marital property assets that are used in an unincorporated business and that are not held by a spouse may be exercised by either spouse, and effective management is determined by possession. *See* Wis. Stat. § 766.51(1)(am); *see also supra* §§ 4.3–.7. Thus, if the business inventory consists of assets that are not held by a spouse, such as animals, steel products, or commodities, either spouse may manage the assets and convey good title to a third party. *See* Wis. Stat. §§ 766.51(1)(am), .57(3). However, a third party may be unwilling to accept an assignment or bill of sale from a spouse who is not active in the business, particularly if that spouse is unable to establish that the inventory or asset being transferred is marital property. If the inventory or asset is not marital property, the inactive spouse would not have the right to manage and control it. *See* Wis. Stat. §§ 766.51(1)(a), .57(3).

## B. Management and Control Remedies [§ 4.77]

If a nonmanaging spouse wishes to obtain management and control rights or is concerned that business assets are being wasted, several procedures may be available to that spouse to protect the marital property assets. *See infra* ch. 8. In addition, if the managing spouse is incompetent, a guardian may be appointed to manage and control the spouse's assets. *See* Wis. Stat. ch. 54.

The Act contains remedies giving a spouse the right to seek to manage marital property assets held in the other spouse's name. One remedy is to add the nonholding spouse's name to the title and thereby obtain the right to manage the property by acting together with the other spouse. *See* Wis. Stat. § 766.70(3). This remedy is not available, however, for any of the following:

1. Assets of an unincorporated business if only one spouse is involved in managing or operating the business;
2. Any general partnership interest, joint venture interest, or interest in a professional corporation, professional association, or limited liability company; or
3. An interest in a closely held corporation.

Wis. Stat. § 766.70(3)(a)–(d).

The add-a-name remedy was not available for interests in a closely held corporation only if the other spouse was an employee of the corporation until the 1988 Trailer Bill removed the employment limitation. *See* Wis. Stat. § 766.70(3)(d) (1985–86). The 1988 Trailer Bill also expanded the business interests to which the remedy under section 766.70(4) is not available to include interests in certain corporations.

The remedy under section 766.70(4) to limit or eliminate a spouse's right to manage marital property assets in the event of gross mismanagement, waste, or absence is generally available if marital property assets have been or are likely to be substantially injured. In this situation the court can also change the classification of an asset, which would change management rights. However, the remedy is not generally available for (1) general partnership interests and joint venture interests,

(2) interests in professional corporations or professional associations; (3) interests in closely held corporations, and (4) any other property if the addition would adversely affect the rights of a third person. *See* Wis. Stat. § 766.70(4)(c). If the remedy is granted by the court, the spouse originally holding the asset could lose all management and control rights.

### **C. Spousal Creditors [§ 4.78]**

The right of a spouse holding a marital property business asset or interest to exclusively manage and control the business asset or interest can be affected by the other spouse's conduct. If the nonmanaging spouse incurs a family-purpose obligation, the obligation can be satisfied from any marital property asset, including an interest in a closely held business. *See infra* § 5.102. Thus, if the nonmanaging spouse defaults on a contract indebtedness or incurs a tort obligation, the creditor can satisfy that obligation from the marital property business interest even though other assets are available for satisfaction. *See infra* § 6.8. This approach differs from the judicially imposed marshalling system in some other community property states, which requires satisfaction from certain assets before others.

### **D. Buy-sell Agreements [§ 4.79]**

#### **1. In General [§ 4.80]**

Frequently, businesses—either corporations or partnerships—use buy-sell agreements to provide a mechanism for the disposition of a stockholder's stock or of a partner's partnership interest in the business. Typically, the agreement provides for the purchase of the interest upon either the death of the owner or an attempted lifetime disposition to a third party. If the owner is an employee of the business, the agreement also frequently provides for purchase upon the employee's retirement or withdrawal.

➤ **Note.** A buy-sell agreement involves at least one third party, another owner or the entity. Section 857.015 is sufficient if the only objective is for the holding spouse to end up as the sole owner of the business interest after the death of either spouse.

Buy-sell agreements can provide for purchase of the interest by the business entity itself or can be structured as a cross-purchase agreement under which one or more shareholders or partners have the right or obligation to purchase. The agreement normally restricts the parties' ability to transfer the business interest outside the contract provisions. If transfers, such as gifts to family members, are permitted, the donees generally must accept the provisions of the agreement as a condition of their receiving the interest. The purchase provision can be mandatory or optional. Frequently, to acquire the funds necessary to make the purchase, the party with the right to purchase obtains insurance on the life of the owner of the business interest.

## **2. Provision Under the Act [§ 4.81]**

The Act contains a provision directed to buy-sell agreements. Section 766.51(9) provides as follows:

If an executory contract for the sale of property is entered into by a person having the right of management and control of the property, the rights of all persons then having or thereafter acquiring an interest in the property under this chapter are subject to the terms of the executory contract. This subsection applies to contracts entered into before or after the determination date.

This provision is not found in UMPA. Clearly, under section 766.51(9), the spouse who holds a marital property business interest has a right, acting alone, to enter into a buy-sell agreement and commit all the marital property interest to the terms of the agreement. The exercise of the management right by one spouse acting alone is subject to the obligation of good faith. *See* Wis. Stat. § 766.15(1). The nonparty spouse's rights in the property disposed of by the agreement attach to the proceeds of the sale; the sale of the stock or partnership interest is not affected by the nonparty spouse's ownership rights in that asset. *See* Wis. Stat. Ann. § 766.51(9) Legis. Council Notes—1985 Act 37, §§ 84 to 87 (West 2009). The statute is significant because it permits a holding spouse to direct a completed purchase of all former marital property stock even though the surviving nonholding spouse may desire to retain his or her one-half interest in the stock as a tenant in common. *See infra* § 12.29.

➤ **Note.** Section 766.51(9) contains a possible oversight in its reference only to interests acquired “under this chapter” (i.e., chapter 766). For example, if the nonholding spouse acquires a marital property interest in the stock or partnership and dies first, leaving a will giving his or her estate to the children, the children obtain one-half of the marital property interest under the Probate Code, not under chapter 766. This appears to be an unintentional drafting error that should not be given substantive effect.

### 3. Classification Issues [§ 4.82]

Section 766.51(9), *see supra* § 4.81, does not eliminate the need to include additional provisions in many buy-sell agreements. To decide whether an existing buy-sell agreement needs revision and the appropriate provisions for new agreements, the classification of the stock or partnership interest must first be determined. Three possible situations exist.

One possible situation involves stock or a partnership interest that was fully paid for and owned before the determination date and therefore is either individual or predetermination date property. If the business interest is individual property, the owner spouse has management and control. *See* Wis. Stat. § 766.51(1)(a). If it is predetermination date property, it is property that would have been either marital property or individual property if acquired after the determination date. During marriage, predetermination date property is treated as if it were individual property, Wis. Stat. § 766.31(9), and management and control rights are determined accordingly. Wis. Stat. § 766.51(1)(a). Although the business interest may be individual or predetermination date property at the outset, a marital property component may arise if, after the determination date, a spouse applies substantial undercompensated efforts to the business and these efforts cause substantial appreciation in the value of the business interest. *See supra* §§ 2.151, 3.45. The mixing of property resulting from a spouse’s effort can be avoided by paying reasonable compensation for the services rendered. *See* Wis. Stat. § 766.63(2). A marital property component may also arise in the business interest if a spouse uses marital property funds to make a capital contribution to the business after the determination date. If no marital property interest arises, a buy-sell agreement entered into by the owner spouse before or after the determination date is fully operative. *See* Wis. Stat. § 766.51(9).

Without the buy-sell agreement, at the owner spouse's death the business interest would become part of that spouse's probate estate, possibly subject to the deferred marital property election. With a buy-sell agreement, the agreement takes precedence. If the spouse who owns the interest dies or if another event triggers the purchase, the agreement applies, and the purchase or option provisions become operative. The deferred marital property election gives an interest in the proceeds, not in the business interest. *See* Wis. Stat. Ann. § 766.51(9) Legis. Council Notes—1985 Act 37, §§ 84 to 87 (West 2009). If the nonowner spouse dies first, no portion of the business interest is included in that spouse's estate. Absent mixing with marital property funds or the application of spousal efforts, the business interest is at most property subject to a deferred marital property election. The deferred marital property election does not apply if the nonowner spouse predeceases the owner spouse. Buy-sell agreements applicable to business interests acquired after the determination date using individual property or predetermination date property funds are likewise fully effective.

A second possible situation involves stock or a partnership interest acquired before the determination date, but with outstanding acquisition indebtedness that is satisfied after the determination date, using marital property funds. Whether the payments after the determination date create a marital property component depends on the mixing rules applied to the transaction in Wisconsin. *See supra* §§ 3.34–37.

A third possible situation involves stock or a partnership interest initially acquired with marital property funds after the determination date. In this situation the stock or partnership interest is classified as marital property, and under the Act, each spouse owns an equal one-half interest. *See* Wis. Stat. § 766.31(3).

#### **4. Consequences When Business Interest Is Partly or Entirely Marital Property [§ 4.83]**

After the stock or partnership interest has been classified and has been found to have a marital property component under the second or third set of circumstances discussed in section 4.82, *supra*, it is necessary to determine whether the spouse holding the interest may, acting alone, enter into a buy-sell agreement governing the entire interest. Regardless of how the business interest is held, if both spouses are parties to the agreement, the agreement should in all cases be sufficient to bind and



obligate their successors in interest. After the determination date, if the stock in a corporation is marital property and is held by only one spouse, that spouse has the exclusive right to manage and control the stock. *See* Wis. Stat. § 766.51(1)(am).

If the business interest subject to a buy-sell agreement is partly or entirely marital property, what happens upon the death of a spouse? If the decedent spouse holds the business interest and is a party to the agreement, no unanticipated consequences should occur, because the death typically triggers a purchase, and section 766.51(9) specifically allows the executory contract to be performed.

However, if the nonholding spouse is not a party to the agreement, and his or her death is not a triggering event, upon his or her death one-half of the marital property component of the business interest is included in his or her probate estate and passes to his or her beneficiaries. The beneficiaries become tenants in common with the surviving spouse. *See* Wis. Stat. § 861.01(2). Typically, the death of a nonholding spouse has not been an event giving rise to any purchase option, especially under agreements entered into before the Act's effective date. Thus, if the beneficiaries of the deceased nonholding spouse are other than the holding spouse, the disposition at death reduces the holding spouse's interest in the business. The beneficiaries of the deceased nonholding spouse's estate ultimately have the right to manage and control the deceased spouse's interest, including the right to vote, or to manage and control the partnership interest or stock received from the estate. The beneficiaries also have the right to receive all distributions from the partnership or corporation in connection with those interests.

The vote of the interest following distribution of the nonholding spouse's estate can be controlled by the holding spouse through the use of a voting trust, notwithstanding beneficial ownership by the beneficiaries of the nonholding spouse. However, the parties to the buy-sell agreement must create the voting trust before the nonholding spouse's death.

If the agreement does not deal with the marital property interest of the nonholding spouse, a further difficult question arises if after the nonholding spouse's death an event such as the death or retirement of the holding spouse triggers a purchase option or obligation. The question is whether the buy-sell agreement is operative as to the stock or partnership interest owned by the beneficiaries of the predeceased nonholding

spouse's estate. Normally, neither the deceased nonholding spouse nor the beneficiaries of his or her estate would be parties to the buy-sell agreement, especially in agreements executed before the Act's effective date. The answer to the above question depends on how the situation is interpreted.

One possible interpretation is that the executory contract created a lien on the stock or partnership interest that passes with the asset to whoever received the asset. This alternative is most likely to apply when the transfer restriction is part of the corporation's articles or bylaws and is reflected on the stock certificate, rather than being merely part of a buy-sell agreement between the corporation and a shareholder or between shareholders alone. *See* Wis. Stat. § 408.204. In any event, however, if the restriction is not reflected on the stock certificate, a third party could purchase the interest and become a bona fide purchaser entitled to unencumbered ownership.

A second possible interpretation is that the buy-sell agreement merely creates a contractual obligation that, to be binding on the beneficiaries, necessitates the timely filing of a contingent claim, on behalf of the other parties to the agreement, in the deceased spouse's estate. This conclusion appears most likely for cross-purchase agreements. It is difficult to find that a lien exists when the certificate on its face does not have any evidence of the agreement.

A third possible interpretation is that the interest is totally unencumbered by the terms of the buy-sell agreement.

The Act does not state which interpretation is the correct one. It appears, however, that for corporate stock, unless the stock is without legend, the third interpretation is the least likely.

Between the spouses these concerns can be resolved by entering into a limited marital property agreement that classifies the stock as the holding spouse's individual property. *See infra* ch. 7. However, since a marital property agreement can be amended by the spouses at any time, the existence of a marital property agreement is not protection for the entity or other shareholders or partners who are parties to the buy-sell agreement. There is a similar lack of protection if the property is held as survivorship marital property.

Accordingly, it is desirable in buy-sell agreements to expressly provide for what happens at the death of the nonholding spouse. At least two approaches can be used:

1. *Grant a first option to purchase.* The holding spouse who is a party to the agreement can provide in the agreement that upon the death of the nonholding spouse, the right exists in the holding spouse or others to purchase all the nonholding spouse's marital property interest. For example, the agreement could grant the holding spouse a first option to purchase, and if the purchase is not made, the agreement could then grant a purchase option to the business entity or, alternatively, to the other parties to the agreement. This appears to be the more desirable alternative if the holding spouse is willing and able to purchase the nonholding spouse's marital property interest if the nonholding spouse dies first. This alternative preserves the right of the holding spouse to vote the entire interest and to receive all distributions, and it keeps the entire interest subject to the buy-sell agreement. Because of the management and control provisions in the statute, this provision can be incorporated in the agreement without the nonholding spouse's consent. The disadvantage of this alternative is that it requires the holding spouse, or other purchasers, to obtain the necessary funds to make the purchase at the nonholding spouse's death, and life insurance is typically not owned on the life of that spouse.
2. *Make the nonholding spouse a party to the agreement.* If the holding spouse is unwilling or unable to purchase the property if the nonholding spouse dies, a second alternative is for the nonholding spouse to be made a party to the agreement. Under the Act, the nonholding spouse does not have power to manage the business interest. *See* Wis. Stat. § 766.51. The right to manage and control an asset includes the ability to sell or transfer the asset. Wis. Stat. § 766.01(11). Even though the nonholding spouse does not have management and control authority under the Act, it appears that the nonholding spouse can contract regarding the subsequent disposition of his or her *ownership interest* in the asset. This includes agreement by the nonholding spouse as to the method of determining the purchase price and the events that will give rise to a sale. The agreement of the nonholding spouse should be binding on his or her transferees. Under this approach the nonholding spouse's interest in the business (including the voting, dividend, and other rights) passes to the beneficiaries of the deceased spouse's estate subject to the

provisions of the buy-sell agreement. The agreement can provide that the stock or partnership interest remains subject to the provisions of the buy-sell agreement so that the interest is sold on the holding spouse's death or on any other triggering event.

➤ **Caution.** The Act may cause an unintended triggering event. Most agreements restrict a party's ability to transfer any part of his or her interest in the business to a third party before the designated triggering event (a prohibited disposition). If the nonparty spouse obtains a marital property interest in the stock, this could violate this restriction and trigger an accelerated purchase. Thus, all agreements should attempt to avoid such unintended results. Existing agreements should be reviewed and possibly amended, and all new agreements should provide that the creation of a marital property interest by itself does not trigger the sale provisions. Normally the parties are not concerned that a marital property ownership interest is created but wish only to limit nonparty spouses from obtaining management and control rights. Thus, in most agreements a solution is to provide that the creation of a marital property interest in the business interest is not a prohibited disposition as long as management and control rights under the Act remain exclusively in the spouse who is a party to the agreement.

## **5. Funding of Buy-sell Agreements with Life Insurance [§ 4.84]**

A final concern relating to buy-sell agreements involves the funding of agreement obligations with life insurance on the lives of the parties to the agreement. *See infra* ch. 10. If the business entity owns such policies, the entity receives the proceeds and can use them to satisfy its purchase obligations under the contract. However, if a cross-purchase agreement is used, the other shareholder or partner owns the life insurance policy. This life insurance is not subject to the special life insurance provisions because it is not an insurance policy insuring the life of the spouse. *See* Wis. Stat. § 766.61(1)(c). It may be subject in part to these provisions, however, if the insured spouse pays any part of the premiums with marital property funds.

➤ **Example.** Assume that a buy-sell agreement is between a father and son, and the son owns a policy on the father's life. If the father

pays a premium, it is either a gift to the son or the payment creates a fractional marital property interest in the policy. In most cases, a gift will have occurred. If not, the marital property interest is owned by the father and his spouse. *See* Wis. Stat. § 766.61(3)(d).

Whether the policy in the above example is also the marital property of the son and his wife is determined under the general classification rules of sections 766.31 and 766.63(1). If the policy on the father's life contains a marital property component between the son and his wife, and the father dies, the proceeds are received by the son and are wholly or partly marital property. The son holds the check and is able to use the funds to satisfy his obligations under the buy-sell agreement. This assumes that the daughter-in-law has not invoked the add-a-name remedy, so that she would be able to hold an interest in the policy and designate the beneficiary of the interest. *See* Wis. Stat. § 766.70(3).

However, if the daughter-in-law in the example dies first, her marital property interest in the policy on the father's life is an asset of her estate. The special purchase provisions of section 766.70(7) do not appear applicable because no marital property funds of the insured father's marriage were used to pay the premiums, and thus the policy is not covered by section 766.61. Thus, the decedent daughter-in-law's marital property interest in the life insurance policy passes to the beneficiaries of her estate, and those beneficiaries are entitled to exercise ownership rights with regard to it, including designation of the beneficiary of that interest. As a result, upon the father's subsequent death, less than the intended proceeds may be paid to the son, who may be less able to fulfill his obligations under the buy-sell contract.

A number of approaches can be adopted to deal with the marital property interest in life insurance.

1. *Use a limited marital property agreement that provides that the life insurance policy is the individual property of the spouse who is a party to the agreement.* This approach makes the entire proceeds available to satisfy the obligation.
2. *Require the insurance in the buy-sell agreement and make both spouses parties to the agreement.* This approach makes both parties personally obligated under the agreement, and thus, if the nonholding spouse dies first, a claim can be filed in his or her estate. *See infra* ch. 10.

➤ **Note.** The insured may be deemed to possess an incident of ownership in the policy if the agreement prohibits a change in beneficiary on the policy. See *Estate of Infante*, 29 Tax Ct. Mem. (CCH) 903 (1970).

3. *Have the nonparty spouse make a gift of his or her interest in the policy to the spouse who is a party to the agreement.*

## VII. Government Benefits [§ 4.85]

### A. In General [§ 4.86]

Two primary questions are involved in dealing with government benefits:

1. Is the amount of benefits payable to a spouse affected by the marital property rule that each spouse has an undivided one-half interest in each spouse's income stream?
2. Is a spouse's qualification for benefits affected by the other spouse's income or assets that exceed the income or asset limitation?

See *supra* § 2.21. A spouse applying for benefits is managing marital property rights. Sections 4.87–.92, *infra*, discuss the likely results for various kinds of benefits.

➤ **Comment.** The effect, if any, of the 2010 health-care reform legislation, the Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010), on Medicare, Medicaid, and other government benefits is not known at this time. Attorneys should check for updates and revisions to the relevant statutes and regulations as the law is implemented.

### B. Federal Old-age, Survivors, and Disability Insurance Benefits [§ 4.87]

The benefits from the Old-age, Survivors, and Disability Insurance program (OASDI), see *generally* 42 U.S.C. §§ 401–434 (Title II of the Social Security Act), are based on the employed spouse's total wage

income, and the Act should not affect qualification for benefits or the amount of benefits. For more information on Social Security, see Social Security Online, <http://www.ssa.gov/>; *see also* 1 Betsy Abramson et al., *Advising Older Clients and Their Families* ch. 8 (State Bar of Wisconsin CLE Books 2d ed. 2007 & Supp.) [hereinafter *Advising Older Clients*]. Further, federal preemption exists, and the benefits are not community property. *Sherry v. Sherry*, 701 P.2d 265, 271 (Idaho 1985).

Under OASDI, benefits are payable to a fully insured individual who has attained age 62. 42 U.S.C. §§ 401–433. To be fully insured, an individual needs to have accrued at least 6 but not more than 40 quarters of coverage (QCs). 42 U.S.C. § 414(a); 20 C.F.R. §§ 404.110, .115. Traditionally, an individual has needed to earn at least a certain amount during each of the applicable quarters to satisfy the QC requirement.

➤ **Note.** Under the current program, since 1978, an individual's total annual earnings are considered in determining how many QCs the individual will be credited with for a given year; consequently, an individual with the requisite annual income may be credited with four full QCs for the year, even though he or she may not have worked during one or more quarters in the year. 42 U.S.C. § 413(a)(2)(A); 20 C.F.R. § 404.140.

The amount of OASDI benefits that an individual is entitled to receive is based on the individual's earnings. 42 U.S.C. § 415; *see also* 20 C.F.R. §§ 404.201–.290 (computing primary insurance amounts). Earnings include wages, *see* 42 U.S.C. § 409, which are defined as remuneration to an employee for employment. 20 C.F.R. § 404.1041(a). Earnings may also include self-employment income, *see* 42 U.S.C. § 411; 20 C.F.R. § 404.1096(a), military wage credits, *see* 42 U.S.C. § 417; 20 C.F.R. §§ 404.1301–.1371, certain railroad compensation, *see* 20 C.F.R. §§ 404.1408, .1027, and wage credits for Japanese-Americans interned during World War II, *see* 42 U.S.C. § 431; 20 C.F.R. § 404.1059. A worker's spouse or dependent child may also be entitled to benefits based on the worker's earning record. 42 U.S.C. § 402.

Individuals who wait until they have reached their full retirement age to begin receiving OASDI benefits will be entitled to their applicable full benefit amount. Full retirement age is currently age 65 but is scheduled to increase incrementally to age 67 by the year 2027. 42 U.S.C. § 416(l). Although an individual may begin receiving OASDI benefits as soon as he or she has attained age 62, *see* 42 U.S.C. § 402(a); 20 C.F.R.

§ 404.310, the benefits received will be less than the amount to which the individual would have been entitled by deferring the receipt of benefits when a beneficiary, who is under the full retirement age or who reaches full retirement age in a given year, has earned income that exceeds a certain amount.

➤ **Note.** Effective January 1, 2000, Congress amended the earnings test to exempt all OASDI beneficiaries who have reached their full retirement age. *See Senior Citizens' Freedom to Work Act of 2000*, Pub. L. No. 106-182, 114 Stat. 198. Before this amendment, beneficiaries were only exempted from the earnings test after reaching age 70.

The auxiliary benefits payable to an employee's spouse or dependent children may also be reduced because of the earnings test. 42 U.S.C. § 403(b).

The OASDI program provides that, in a community property jurisdiction, when spouses have a trade or business other than a partnership, the gross income and deductions are attributed in most circumstances to the spouse carrying on the trade or business. If the trade or business is jointly operated, the gross income and deductions are attributed to each spouse on the basis of their respective distributive share of the gross income and deductions. 42 U.S.C. § 411(a)(5)(A).

### **C. Health Insurance for the Aged and Disabled: Medicare [§ 4.88]**

If an individual is age 65 and is eligible for OASDI benefits or auxiliary benefits, he or she is eligible for Medicare. 42 U.S.C. §§ 426, 1395c. *See generally 2 Advising Older Clients, supra* § 4.87, ch. 10 (detailed discussion of Medicare). Thus, the Act does not affect Medicare eligibility. Nor are Medicare benefits affected by the Act. Those benefits are based on hospital and other medical costs and are not tied to the recipient's assets or income. 42 U.S.C. §§ 426, 1395d.

### **D. Unemployment Insurance [§ 4.89]**

Unemployment insurance is a state-administered program that is funded in part by the federal government. Eligibility and benefit



calculation standards are essentially set by the state. The Wisconsin statute provides that “[b]enefits shall be paid to each unemployed and eligible employee.” Wis. Stat. § 108.03(1). The term *employee* is defined, in part, as “any individual who is or has been performing services for an employing unit.” Wis. Stat. § 108.02(12)(a). The applicant’s marital property interest in his or her spouse’s wages does not affect eligibility. See Wis. Stat. §§ 108.04 (eligibility for benefits), .02(4m) (base period wages). Thus, qualification is not affected by the Act.

The amount of benefits is based on the eligible employee’s average quarterly wage. Wis. Stat. § 108.05. Wages are defined as remuneration for personal services. Wis. Stat. § 108.02(26). Under this definition of wages, the Act has no effect on the amount of unemployment insurance benefits paid to an employee spouse.

### **E. Supplemental Security Income for Aged, Blind, and Disabled [§ 4.90]**

Supplemental Security Income (SSI) is a federally administered program for aged, blind, and otherwise disabled persons with few or no resources. See generally 42 U.S.C. §§ 1381–1383f (Title XVI of the Social Security Act); 1 *Advising Older Clients*, *supra* § 4.87, ch. 9 (detailed discussion of SSI). The states are permitted to institute additional supplemental payment programs. 42 U.S.C. § 1382e; Wis. Stat. § 49.77. Under SSI, an applicant’s benefit is based on the cost of living for an individual, or if he or she is married, on the cost of living for a couple. 42 U.S.C. § 1382(b). For married individuals, all income of both spouses is counted in determining eligibility. 42 U.S.C. § 1382(a)(2). There is also a limit on resources, which is computed differently depending on whether an individual or a couple is applying for benefits. *Id.* Because all income and assets of both spouses are considered, the Act should not affect eligibility.

States may adopt a supplemental program providing greater benefits or lower standards for qualification. California, for example, has adopted a program that provides supplemental benefits. One of the factors considered in calculating eligible income levels for married applicants under that program was challenged in a class action in *Disabled & Blind Action Committee v. Jenkins*, 118 Cal. Rptr. 536 (Ct. App. 1974). The court held that in determining a married applicant’s

eligibility for the supplemental program, all the noneligible spouse's income must be considered. The court pointed out that the legislature could have excluded consideration of spousal income but chose not to do so. A concurring opinion stated that, rather than considering all the ineligible spouse's income, only the applicant's one-half interest should have been considered. *Id.* at 547–48 (Friedman, acting P.J., concurring).

## **F. Personal Responsibility and Work Opportunity Reconciliation Act [§ 4.91]**

The program providing aid to families with dependent children (AFDC) was restructured by the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, Pub. L. No. 104-193, 110 Stat. 2105, which replaced the program with block grants to the states to provide temporary assistance to needy families. *See* 42 U.S.C. §§ 601–619. The Wisconsin plan, Wisconsin Works (W-2), is set forth in sections 49.141–.161. Eligibility for benefits considers the income of both spouses if they live in the same home as the dependent child. Wis. Stat. § 49.145(3)(b). In other situations, spousal income is not considered. Only the income of a parent is considered and, thus, stepparent income should not be considered.

An applicant's need is determined by the number of family members and area shelter costs. Wis. Stat. §§ 49.141, .19(11). If an applicant's total income, earned and unearned, exceeds 185% of the standard of need, or if the total earned and unearned income after disregarded items are applied exceeds 100% of the standard of need, the family is ineligible. Wis. Stat. § 49.19(4)(es).

## **G. Medicaid—Title XIX [§ 4.92]**

Medicaid is the chief welfare medical assistance program under the Social Security Act. *See generally* 42 U.S.C. § 1396–1396v; 2 *Advising Older Clients*, *supra* § 4.87, ch. 11 (detailed discussion of Medicaid). It is a state-administered program with partial federal funding. Medicaid is available to recipients of Social Security aids, such as SSI and aid to families with dependent children, and to certain other individuals. Wis. Stat. § 49.46(1). Thus, eligibility is not affected by the Act. *See supra* §§ 4.90, .91.

In addition, Medicaid is available to certain persons who are medically indigent. Wis. Stat. § 49.47. A person is medically indigent if his or her property does not exceed certain amounts (with separate amounts depending on family size) and his or her income does not exceed limits that are tied to SSI and AFDC. *See* Wis. Stat. § 49.47(4). These programs consider the nonapplicant spouse's income.

A Wisconsin circuit court considered whether a veteran's disability pension and a civil service pension are classified as marital property or whether federal preemption applies and precludes division of those benefits. *Yde v. Yde*, No. 740-850 (Wis. Cir. Ct. Milwaukee County Dec. 18, 1987). In this case, the benefit recipient was receiving Medical Assistance and was required, as a condition of Medical Assistance, to turn over all his income to the veterans home. The court held that, because of federal preemption, the benefits could not be classified as marital property and thus were not divisible between the spouses. *Id.*

Once an applicant qualifies for Medicaid, the benefits, like Medicare, are based on care costs and are subject to payment limitations. Wis. Stat. § 49.46(2). Thus, the benefit levels are not affected by the applicant's interest in marital property income.

In administering this program, the federal Secretary of Health and Human Services has developed a rule known as the "name-on-the-check" rule for determining an applicant's available income. Under this rule, when one spouse is in a nursing home and the other resides in a private residence, the name on the check determines the income of the nursing home resident. The Supreme Court of Louisiana has considered this rule and the resulting preemption of its community property laws. *In re Hamner*, 427 So. 2d 1188 (La. 1983). In that case, the husband was denied Medicaid assistance because his retirement income exceeded the federal eligibility standard (300% of the SSI benefit amount). The trial court ruled that under Louisiana community property law, the husband and his wife each owned an equal share in the husband's retirement income. Thus, the court held that the husband was entitled to only one-half of such income, and since his one-half of the total income met the test, he qualified for Medicaid assistance. The Louisiana Supreme Court reversed the ruling and held that all the income received in the husband's name should be considered. The court found that Congress intended uniform national standards of eligibility for medical benefit programs. Variations should not be allowed to develop because some states have community property and others do not.

Two decisions involving Washington law reached the opposite result. In *Purser v. Rahm*, 702 P.2d 1196 (Wash. 1985), the court noted that the income rule was not contained in the federal statutes or regulations but was merely a practice of the Washington Department of Social and Health Services, based on the department's interpretation of federal law. The court reasoned that for a federal law to preempt state community property law, the state property law must do major damage to clear and substantial federal interests. *Id.* at 1199. Because the Medicaid statute did not set a criterion for determining ownership of income, the court ruled that substantial federal interests were not affected. The court noted that community property law was used in determining eligibility for AFDC and stated that this fact strongly supported its use in determining Medicaid eligibility. The court further stated that application of community property law "does not have a disproportionately negative impact on the intended beneficiaries of Medicaid." *Id.* at 1203. The court rejected the analysis in *Hamner* as being incorrectly based on the uniformity provisions of the Medicaid statute. Thus, the court applied community property ownership rules in determining Medicaid eligibility.

Before the Washington Supreme Court's decision in the *Purser* case, the state of Washington submitted to the federal Secretary of Health and Human Services a proposal to amend the Washington statutes to use community property laws rather than the name-on-the-check rule to determine income eligibility. The Secretary denied the application, and the state challenged the denial in *Washington Department of Social & Health Services v. Bowen*, 815 F.2d 549 (9th Cir. 1987). The court found that most elderly couples received more income in the husband's name than the wife's name. The court also found that the name-on-the-check rule is an administrative interpretation of a Medicaid regulation. *Id.* at 553. In cases involving elderly spouses, income of the nonapplicant spouse is often deemed the applicant spouse's income after the period for attribution has expired; this is contrary to legislative intent. In addition, the court found the Washington proposal less restrictive in eligibility than the secretary's rule, and there was a legislative moratorium in effect preventing denials of expanded coverage. Finally, the court said that "[s]tate family property law cannot be preempted by federal law ... unless 'Congress has positively required [preemption] by direct enactment.'" *Id.* at 556. Thus, the Washington proposal was approved.

California submitted a similar proposal to apply community property laws to determine eligibility; this proposal was also rejected by the Secretary of Health and Human Services. The rejection was challenged

in *Department of Health Services v. Secretary of Health & Human Services*, 823 F.2d 323 (9th Cir. 1987). The court made the same analysis as in *Bowen* and found *Bowen* controlling in the Ninth Circuit. Thus, the court approved the California proposal to determine eligibility consistent with its community property law.

➤ **Comment.** Whether the Act affects Wisconsin residents' eligibility for Medicaid depends on the final resolution of whether the federal name-on-the-check rule preempts Wisconsin marital property law.



## Obtaining and Granting Credit

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## I. Common-Law Experience [§ 5.1]

### A. Basis of Credit System [§ 5.2]

#### 1. Marriage Relationship Generally Irrelevant [§ 5.3]

With the exceptions noted in section 5.4, *infra*, the existence of the marriage relationship is irrelevant for the purpose of obtaining or granting credit in common-law states. A spouse's ability to contract for debt, and hence to obtain credit, generally depends on that spouse's income and property, taking into account his or her personal liabilities. *See* W.S. McClanahan, *Community Property Law in the United States* §§ 2:23, 10:1 (1982). It does not generally depend on the marriage relationship or the other spouse's assets, income, or liabilities. *Id.*<sup>1</sup>

Similarly, with the exceptions noted in section 5.4, *infra*, a creditor in a common-law state may satisfy a debt incurred by one spouse only from that spouse's personal assets and income; the creditor may not collect from the assets or income of the spouse who did not incur the debt.

The nonincurring spouse may voluntarily alter this situation, however. This may happen in one of two ways. First, the spouse may join in or guarantee the credit instrument involved. Personal liability of that spouse would result, and the creditor could proceed against the income and assets of either spouse. Second, by executing a security agreement, the nonincurring spouse can grant a security interest in assets titled in his or her name. Those assets of the nonincurring spouse would be available to satisfy the obligation secured, although personal liability would still be limited to the debtor spouse. In either case, the additional

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189, all references to the United States Code (U.S.C.) are current through Public Law No. 111-154 (excluding Pub. L. Nos. 111-148, 111-152) (Mar. 31, 2010), all references to the Code of Federal Regulations (C.F.R.) are current through 75 Fed. Reg. 17,023 (Apr. 2, 2010), and all references to the Wisconsin Administrative Code are current through rules promulgated in the Wisconsin Administrative Register, No. 652, Apr. 30, 2010 (effective May 1, 2010). Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

liability or the availability of additional assets to satisfy an obligation is based on contract, not on the marital relationship of the spouses. The joinder or grant of a security interest is voluntary on the part of the nonincurring spouse and therefore subject to that spouse's control.

Under the common-law property system outlined above, if one spouse owns more property or earns more income, that spouse may control both spouses' access to credit and thus generally will wield greater influence over the spouses' mutual economic destiny.

## **2. Exceptions [§ 5.4]**

In common-law property states, there are certain limited exceptions to the general rule that the marriage relationship is irrelevant for the purpose of obtaining or granting credit. These exceptions generally fall into two categories: obligations based on the duty of support and obligations based on the doctrine of necessities. *See infra* §§ 5.105–.110. Under these exceptions, the nonincurring spouse may be personally liable for the credit obtained by the incurring spouse.

Common-law property states also have various joinder rules requiring the spouses to act together with respect to some types of assets, such as the homestead. *See infra* §§ 5.16, .134. In addition, certain assets held by spouses may be exempt from execution by judgment creditors and therefore unavailable for consideration in obtaining credit. *See infra* §§ 5.39, 6.30.

## **B. Equal Access to Credit [§ 5.5]**

One significant criticism of the common-law system is spouses' lack of equal access to credit based on marital assets and the income stream of both spouses. In fact, a major goal of the Uniform Marital Property Act (UMPA), which is reprinted in appendix A, *infra*, was to ensure such equal access to credit. As characterized by one commentator, UMPA “should function so that each marital partner may obtain unsecured credit backed by the entire pool of marital assets. A potential for increased trading arises with the advent of an additional marital partner with full power to charge against the interests of both participants.” Richard V. Wellman, *Third Party Interests Under the Uniform Marital Property Act*, *Uniform Marital Property Act Symposium*, 21 Hous. L. Rev. 717 (1984).

In Wisconsin, a recurring argument made by the proponents of marital property reform was that spouses who earned no wages or lower wages than their marriage partners, as well as spouses with no assets or fewer assets than their marriage partners, were being unfairly denied access to credit. Regarding the prohibition in section 138.20 against discrimination in the granting of loans or credit, see section 5.57, *infra*. Regarding the rules promulgated by the Wisconsin Division of Banking in connection with discrimination in the granting of credit, see section 5.58, *infra*. In position papers and legislative hearings, the Wisconsin Marital Property Act, 1983 Wis. Act 186, by which a form of community property ultimately was adopted in Wisconsin, was presented as the means to achieve equal access to credit by Wisconsin spouses. See Wis. Stat. § 766.001(2) (stating legislative intent that marital property is form of community property); see also *infra* § 5.60 (purpose and intent of Act in connection with obtaining credit). The bulk of the Wisconsin Marital Property Act (or the Act) is codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes.

## **II. Community Property Fundamentals [§ 5.6]**

### **A. In General [§ 5.7]**

To understand the system for obtaining and granting credit under the Wisconsin Marital Property Act, one needs a general understanding and appreciation of the basic concepts and historical background of community property. This is because a number of concepts from other community property states were incorporated into UMPA and, from there, into Wisconsin's Act. However, the Wisconsin Marital Property Act also contains unique provisions relating to credit not found in UMPA or in the laws of any other community property state. Anyone researching the cases from other community property states or the comments to UMPA will therefore need to be aware that, despite basic similarities, significant differences do exist among the community property states and between UMPA and the Wisconsin Marital Property Act. See, e.g., *infra* §§ 5.14, .18.

### **B. Basic Concepts [§ 5.8]**

Under a community property system, a theory of a separate community entity can be useful in analyzing debts and creditors' rights.

Under this theory, community property assets are sometimes viewed as owned by the community, a type of legal person or entity with the power to incur debts. The concept of a community entity is analogous to that of a partnership that is treated as an entity separate from its partners. McClanahan, *supra* § 5.3, § 10:2. It is interesting to note that—as a reflection of the independent nature of the community entity—under the federal Bankruptcy Code, even if only one spouse is in bankruptcy, generally all community property is brought into the bankruptcy estate and all community debts may be filed as claims. *Id.* § 10:10; *see infra* §§ 6.72–.77.

Under historic community property concepts, many of which still apply in community property states, obligations are classified to determine which spouse is personally liable for them and which assets may be reached to satisfy them. McClanahan, *supra* § 5.3, §§ 10:3–10:4; *see also* Michael J. Vaughn, *The Policy of Community Property and Inter-Spousal Transactions*, 19 Baylor L. Rev. 20, 60 (1967). An obligation may be classified as a community debt, the husband's separate debt, or the wife's separate debt. With respect to assets that may be reached, community property generally is available to satisfy community debts, and each spouse's separate property is available to satisfy each spouse's separate debts. Further rules govern which spouse can incur a community debt.

Different community property states have dealt with the acquisition of credit by spouses in different, and sometimes inconsistent, ways. Similarly, different community property states have taken a variety of approaches to the rights of creditors to reach community and separate property assets.

A leading casebook characterizes California, Idaho, Louisiana, Nevada, and Texas as following a *managerial system* for determining liability to a creditor. *See* William A. Reppy Jr. & Cynthia A. Samuel, *Community Property in the United States* 251–55 (2d ed. 1982). That is, the property (community or separate) that a spouse has the authority to manage is available to repay the obligations incurred by that spouse. Such availability is in addition to the personal liability of that spouse. Under the managerial system, the rights of creditors do not depend on whether the obligation was incurred for a separate or a community purpose. It is important to note, however, that there are a number of exceptions to these rules in the managerial system. The exceptions

include the necessities doctrine, the duty of support, and the family-purpose doctrine. *See infra* §§ 5.29–.39, .105–.110.

Another approach to obtaining and granting credit that some community property states follow is based on a *community debt system*. The previously cited casebook characterizes Arizona, Washington, and New Mexico as following this approach. *See* Reppy & Samuel, *supra*, at 255–67. Under the community debt system, debts generally are classified as separate or community when the creditor seeks payment, with the debt’s characterization determining the property the creditor can reach.

UMPA, on the other hand, has been characterized as neither a purely managerial nor a purely community debt system; rather, it appears to contain elements of both, with a number of compromises. *See* Wellman, *supra* § 5.5, at 738–41.

### **C. Family-purpose Doctrine [§ 5.9]**

A doctrine has developed in some community property states—notably Arizona, Louisiana, and Washington—that obligations resulting from a contract made on behalf of the community are community obligations. *See* Reppy & Samuel, *supra* § 5.8, at 265 n.2; UMPA § 8 cmt. Similarly, under this doctrine, judgments arising from torts committed while a spouse was attempting to benefit the community are community obligations. *See* McClanahan, *supra* § 5.3, § 10:4, at 485–86; *see also* William Q. de Funiak & Michael J. Vaughn, *Principles of Community Property* § 182, at 432–33 nn.1–3 (2d ed. 1971). Known as the *family-purpose doctrine*, this doctrine sometimes is buttressed by a presumption that a debt incurred by a spouse was incurred for a family purpose and hence is a community obligation. *See* UMPA § 8 cmt. Thus, in general, in addition to the separate property assets of the debtor or tortfeasor spouse, community property assets can be reached by the creditor to satisfy a community obligation.

### **D. Management and Control as Basis of Credit [§ 5.10]**

In most community property states, the ability to contract for debt, and correspondingly, creditors’ ability to collect, are now based primarily on a spouse’s power of management and control. *See*



McClanahan, *supra* § 5.3, § 9:9.a. *See generally* de Funiak & Vaughn, *supra* § 5.9, §§ 111–130. Historically, however, the husband was the sole manager of the community (and sometimes of his wife’s separate property as well). The husband’s authority as manager rendered him analogous to a partner or an agent for the community. His authority included the power to manage, possess, convey, and encumber community property and enter into contracts binding on the community. However, these powers were subject to a type of fiduciary duty requiring the husband, as manager of the community, to act only for the benefit of the community or the spouses. McClanahan, *supra* § 5.3, § 9:1.

Eventually, the rule that the husband was the sole manager of the community was altered by legislative enactments, the first significant variation being the statutory changes Texas made in the late 1960s to provide for separate management of community property by the spouses. *Id.* § 9:8, at 450, 452; *see also* Reppy & Samuel, *supra* § 5.8, at 205, 228–32. This change granted each spouse sole management powers over that part of the community property he or she would have owned absent the marriage. With respect to assets that had become commingled, dual management applied.

Between 1972 and 1980, other community property states adopted equal-management statutes. *See* McClanahan, *supra* § 5.3, § 9:12. In general, these statutes grant spouses a concurrent right to act unilaterally to bind community property, except for real estate, which requires concurrent action (dual management). Various exceptions to these rules exist in the community property states.

Finally, with respect to credit, the management power provided under the equal-management system usually includes the power of either spouse to obtain credit and to incur liability on behalf of the community, in addition to the power to encumber community assets. The statutes in various community property states contain exceptions that require (1) concurrent action (dual management) or joinder under certain circumstances (such as when real property is involved), and (2) sole management under other circumstances (such as when management of business assets is involved).

## **E. Effect of Equal Management Statutes on Credit [§ 5.11]**

Under equal-management statutes, each spouse is granted the right to independently create community debts and obtain credit accordingly on the basis of community assets. *See* John A. Adamske, *Equal Management and Control in California*, 2 Comm. Prop. J. 25, 29–32 (1975). In theory, this should promote greater access to credit by spouses. However, the joinder rules, various “commercial practicality” exceptions, and a carryover of earlier attitudes have limited equal access to credit in practice. *See* Anne K. Bingaman, *Equal Credit Opportunity: The Impact of Equal Management of Community Property*, 4 Comm. Prop. J. 157 (1977). *See generally infra* §§ 5.95–.96 (federal Equal Credit Opportunity Act joinder rules).

Equal access to credit is also limited by the fact that a number of the states with equal-management statutes rely on documents of title. *See* McClanahan, *supra* § 5.3, § 9:14.a (titled property); Reppy & Samuel, *supra* § 5.8, at 206–08; *see also* McClanahan, *supra* § 5.3, § 9:13 (business interests). For example, in Louisiana, sole management is vested in the “title owner” of “movables,” including automobiles, securities, insurance policies, and certain bank accounts. Similar exceptions exist in New Mexico. In Texas, a presumption that sole management applies is based on title, or on possession in the case of assets not subject to title evidence. Likewise, various presumptions of sole management arise based on record title in California and Washington. *See* McClanahan, *supra* § 5.3, § 9:14.

## **III. Wisconsin Marital Property Act Approach: Overview [§ 5.12]**

### **A. In General [§ 5.13]**

Credit is one of the areas of law most affected by the Wisconsin Marital Property Act. Although the Act did not significantly change the personal liability aspects of the credit system in Wisconsin, the general approach to obtaining and granting credit by married persons has been fundamentally altered.

Two factors lie at the heart of creditor-debtor relationships under the Act, particularly in unsecured credit transactions:

1. The Act's adoption of the family-purpose doctrine; and
2. The concept that specific classes of property are "obligated" for nontort debts, in the sense that such property may be reached by the creditor to satisfy certain obligations, independent of personal liability.

*See infra* §§ 5.29–.39. Classes of property are available to satisfy an obligation based on the category of the obligation rather than simply on the personal liability of the owner of the property. In fact, marital property assets may be available as the result of a credit transaction of one spouse, without any personal liability for the other spouse who is, of course, the owner of a one-half interest.

The provisions of the Act that result in specific classes of property becoming obligated are based on the UMPA *creditors' remedy approach* to obtaining and granting credit. Under that approach, an essential element in obtaining and granting credit is the extent of the assets or income the creditor is able to reach to satisfy the debt. In addition to the UMPA approach, the Act adopts specific, detailed provisions governing credit transactions with married persons. *See infra* §§ 5.19, .41–.104.

Another concept adopted by the Act but not in UMPA is that of expanded application of management and control of marital property assets for the purpose of obtaining credit. When a family-purpose obligation is involved, the system for obtaining unsecured credit under the Act (and secured credit when purchase money security interests are involved) is based on the concept of a spouse's expanded rights of management and control of marital property assets in credit transactions. The Act expands the application of management and control rights in such credit transactions beyond those provided in UMPA. *See infra* §§ 5.15, .41–.75.

With respect to secured transactions, the credit system under the Act is based on the Act's concepts of management and control of marital and nonmarital property assets (excluding the expanded application of management and control under section 766.51(1m)). *See infra* §§ 5.15, .16, .89. With respect to granting a security interest in a purchase money secured transaction, see section 5.25, *infra*.

## B. Management and Control Rights [§ 5.14]

### 1. In General [§ 5.15]

Under the Act (as under other community property systems), management and control rights, and in most cases even title, do not affect classification (i.e., ownership) of property. *See* Wis. Stat. § 766.51(5). Nor do these rights rebut the presumption under section 766.31(2) that all property of spouses is presumed to be marital property. Wis. Stat. § 766.51(5); *see de Funiak & Vaughn, supra* § 5.9, § 102; *see also supra* § 2.26. Management and control rights do apply, however, in credit transactions. Under the Act, spouses, acting alone or together, have certain rights to enter into credit transactions affecting marital property assets over which they have rights of management and control. Section 766.01(11) defines *management and control* as “the right to buy, sell, use, transfer, exchange, abandon, lease, consume, expend, assign, create a security interest in, mortgage, encumber, dispose of, institute or defend a civil action regarding or otherwise deal with property as if it were property of an unmarried person.”

➤ **Note.** With respect to management and control rights generally, *see* chapter 4, *supra*.

In addition to the management and control rights discussed in this section and section 5.16, *infra*, spouses are granted expanded management and control rights to incur credit for family-purpose obligations. *See infra* §§ 5.41–.75.

### 2. Sole Management and Control [§ 5.16]

Based on concepts of title or how the property is “held,” each spouse has sole management and control rights under section 766.51(1)(a)–(f) in third-party transactions, including those involving secured and unsecured credit, with respect to the following items of property:

1. *That spouse’s property that is not marital property.* Each spouse may manage and control, by his or her sole action, his or her individual property assets and his or her other nonmarital property assets (i.e., predetermination date property, *see supra* § 2.13). As to predetermination date property, section 766.51(6) specifically

provides that the enactment of the Act does not affect the right to manage and control such property. As to such property held in joint tenancy or tenancy in common, the normal rules of title-based management in effect before the determination date apply. *See supra* chapter 4.

2. *Marital property assets held in that spouse's name alone or marital property assets that are not held in the name of either spouse (i.e., nontitled property).* Regardless of the other spouse's ownership interest in the assets, marital property assets held (or titled) in only one spouse's name may be used by that spouse for secured or unsecured credit purposes as if the property were owned by an unmarried person. Under this rule, both the management and control rights of the title-holding spouse and the rights of bona fide purchasers are unaffected by either (a) a claim by the other spouse, such as for mismanagement in violation of the good-faith duty under section 766.15, or (b) an objection by the other spouse to a particular transaction. The other spouse's claim is limited to his or her remedy against the managing spouse. *See Wis. Stat. §§ 766.70 (interspousal remedies), .57 (protection of bona fide purchasers dealing with spouses); see also supra* ch. 4, *infra* ch. 8. Similarly, marital property assets not held in the name of either spouse (such as bearer bonds, jewelry, or a coin collection) may be used for credit purposes by the spouse having possession as if they were owned by and in the sole possession of an unmarried person. A creditor dealing with a spouse having management and control rights is protected, assuming the requirements for a bona fide purchaser are met. *See infra* § 5.28; *see also supra* § 4.4.
3. *Marital property assets held in the names of both spouses in the alternative.* The Act provides that marital property assets may be held in the alternative (the "or" form). *See Wis. Stat. § 766.60(1)*. In that case, either spouse acting alone has full rights of management and control and may deal with the property, for secured or unsecured credit purposes, as if it were held solely in that spouse's name. With respect to property in this category, creditors are afforded the same protection as when property is held solely in the applicant spouse's name. *See infra* § 5.28.
4. *A policy of life insurance, when that spouse is designated as the owner on the insurance company's records.* With respect to life insurance, the rule of item 2. above applies. That is, the spouse may

use the life insurance policy for credit purposes as if the spouse were unmarried. The life insurance company's protection is similar to that of a bona fide purchaser; it is protected when dealing with the person named as owner on its records unless it has actual knowledge of an inconsistent decree, agreement, or adverse claim. *See* Wis. Stat. § 766.61(2).

5. *Any right of an employee under a deferred-employment-benefit plan.* As with life insurance, the rule of item 2. above applies, and the administrator of a deferred-employment-benefit plan is protected if the administrator acts in accordance with the plan and the administrator's records. *See* Wis. Stat. § 766.62(4). With respect to tax-qualified retirement plans (and possibly other plans as well), the application of spendthrift provisions and the effects of the Employee Retirement Income Security Act of 1974 (ERISA) and other applicable federal and state laws may affect the extent of the spouse's management and control rights. *See supra* §§ 2.184–.218, 4.25.
6. *A claim for relief vested in that spouse by other law.* The rule of item 2. above also applies to this situation.

### **3. Joint Management and Control [§ 5.17]**

The rules of management and control described in section 5.16, *supra*, permit one spouse to act alone; in contrast, spouses have joint management and control rights over marital property assets held in the names of both spouses, other than in the alternative form. Section 766.51(2) provides that when marital property assets are held in both names (not in the alternative), the assets may be managed and controlled only by the spouses acting together. Joint action also is required for certain transactions involving the homestead. *See* Wis. Stat. § 706.02(1)(f); *see also infra* § 5.134 (joinder in connection with homestead).

These management and control rights apply in all nontort transactions with third parties, including secured and unsecured credit transactions.

## C. Nature of Marital Property Subject to Management and Control and Required to Be Considered in Credit Transactions [§ 5.18]

### 1. In General [§ 5.19]

From a creditor's perspective (and consequently from the perspective of a spouse seeking credit), an essential element in granting credit is what assets or income the creditor can reach to satisfy the resulting debt. UMPA bases its system for obtaining and granting credit on this essential element and is therefore remedy-oriented. *See supra* § 5.13. Under the UMPA system, if an obligation comes within the family-purpose doctrine, all marital property assets can be reached to satisfy the obligation; in addition, the creditor can reach the individual and other nonmarital property assets of the incurring spouse, based on that spouse's personal liability.

The Wisconsin Marital Property Act adopts the same basic approach. For instance, consistent with UMPA's creditors' remedy approach, in credit transactions with a spouse involving a family-purpose obligation, the Wisconsin Act requires the creditor to consider all marital property assets available to satisfy a family-purpose obligation in evaluating the spouse's creditworthiness. *See* Wis. Stat. § 766.56(1).

➤ **Note.** Although consistent with UMPA, the approach of the Wisconsin Act goes beyond UMPA's approach by *requiring* such consideration rather than merely relying on what the creditor may consider to be in the creditor's own interest.

Although UMPA and the Wisconsin Act follow the same basic approach to credit, the sponsors of the Act apparently concluded that sole reliance on the UMPA approach was insufficient to obtain the goal of equal access to credit by each spouse. *See* Lynn Adelman et al., *Departures from the Uniform Marital Property Act Contained in the Wisconsin Marital Property Act*, 68 Marq. L. Rev. 390 (1985); *infra* § 5.42. As a result, in addition to the UMPA creditors' remedy approach, the Act relies on the concept of management and control by spouses in credit transactions. This was accomplished, first, by expanding the application of management and control in unsecured family-purpose credit transactions in section 766.51(1m), and second, by creating entirely new sections concerning credit transactions with

married persons, *see* Wis. Stat. §§ 766.555, .56, .565. *See infra* §§ 5.14–.17, .41–.104.

The Act's addition to UMPA of the expanded application of management and control rights in unsecured credit transactions, and its addition of new procedures concerning credit transactions with spouses, were not accompanied by explicit changes in UMPA's corresponding sections dealing with the assets or income an unsecured creditor may reach to satisfy the resulting obligation. However, since the expanded management and control rights apply only in unsecured credit transactions when a family-purpose obligation is involved, and since the requirements for evaluation of creditworthiness (involving attribution of marital property assets to the spouse applying for credit, *see infra* §§ 5.52–.55) apply only to the extent that the marital property assets can be reached to satisfy the family-purpose obligation, there appears to be no conflict or inconsistency.

➤ **Note.** There is an inconsistency between section 766.51(1m)(b) and section 766.55(2)(b). Even though management and control rights in marital property business assets are restricted under section 766.51(1m)(b), the excepted marital property assets are nevertheless available to the creditor of a family-purpose obligation under section 766.55(2)(b). *See infra* § 6.8.

With respect to secured credit, the creditor may rely on the normal management and control rules in section 766.51—that is, the rules other than those under section 766.51(1m)—to determine whether the debt-incurring spouse has the power to grant a security interest in the particular marital property assets. *See infra* §§ 5.129–.135.

However, particularly in circumstances involving unsecured credit, it is necessary to determine the scope of the term *property*, as used in the credit sections that were added to UMPA by the Wisconsin Act. In this context, the UMPA definition of property was not modified. The expanded application of management and control rights applies to marital property, and the attribution of creditworthiness is based on marital property. The scope of the term property is especially significant with respect to the property nature of future income in the credit context. *See infra* § 5.23.



## **2. Marital Property Broadly Defined [§ 5.20]**

The Marital Property Act defines *marital property* in the broadest possible terms. For purposes of the Act, the term property is defined to mean “an interest, present or future, legal or equitable, vested or contingent, in real or personal property.” Wis. Stat. § 766.01(15). Further, the Act is subject to a rule of liberal construction; section 766.001(1) states that “[t]his chapter is remedial in nature and shall be liberally construed.” The Act also is to be construed to promote an intent “to recognize the valuable contributions of both spouses during the marriage and at termination of the marriage by dissolution or death.” Wis. Stat. § 765.001(2). (Section 765.001(2) applies by its terms to chapters 765–68.) Finally, the Act promotes the principle that “[u]nder the laws of this state, marriage is a legal relationship between 2 equal persons.” *Id.*

## **3. Future Earned Income [§ 5.21]**

### **a. In General [§ 5.22]**

As noted in section 5.19, *supra*, the scope of the term property under the Act is especially significant with respect to the nature of future income in the credit context. Because of the importance of a spouse’s future income stream in obtaining credit, and because of the previously mentioned expanded application of management and control rights in credit transactions under section 766.51(1m) and the attribution of creditworthiness under section 766.56(1), *see supra* § 5.19, it may be necessary to determine whether, under the Act, the spouses’ future earned income is marital property subject to the expanded management rights. It also may be necessary to determine whether future earned income of the nonapplicant or nonobligated spouse is marital property for purposes of management and control and attribution of creditworthiness. This inquiry is also necessary under the federal Equal Credit Opportunity Act. *See infra* §§ 5.77, .92–.96; *see also infra* § 5.94 (discussing *United States v. ITT Consumer Finance Corp.*, 816 F.2d 487 (9th Cir. 1987), holding that, under state law of seven community property states involved, creditors may not be required to consider future income of nonapplicant (nonobligated) spouse in determining creditworthiness of applicant spouse because such future income is not community property until earned).

Two background points relevant to the question of whether future income is marital property under the Act must be made. First, consideration of the nature of marital property does not, for these purposes, relate to what property can be “held.” *See supra* §§ 2.19, 4.5. Instead, it relates to broader questions, namely the following:

1. What property is subject to management and control under the expanded application of section 766.51(1m), for the purpose of obtaining an extension of credit for a family-purpose obligation?
2. Is future income generated by the nonapplicant spouse property to be considered in attributing creditworthiness under section 766.56(1)?

Second, in evaluating creditworthiness, reliance is placed on the family-purpose doctrine, regardless of whether the spouses’ future income constitutes property for management and control purposes. *See infra* § 5.31. Section 766.55(2)(b) fully retains UMPA’s remedy approach based on the family-purpose doctrine. *See supra* § 5.13.

## **b. Nature of Future Income in Property Law Context [§ 5.23]**

For property law purposes, future income from personal efforts does not constitute property under the Wisconsin Marital Property Act. *See infra* § 5.20 (regarding broader definition); *see also infra* §§ 5.91–.96 (applicability of Equal Credit Opportunity Act). *See also In re Pietri*, 59 B.R. 68 (Bankr. M.D. La. 1986), discussed at section 6.82, *infra*.

Although section 766.01(15) defines property in the broadest possible terms to include an interest—present or future, legal or equitable, vested or contingent—in real or personal property, the import of the Act is that, to constitute property, income from services or efforts first must be earned or accrued. Further, it appears that a marital property interest cannot exist until an asset (such as cash or a transferable item) exists or until the right to receive the asset has accrued. At that point, the interest is classified as marital property, individual property, or other (i.e., predetermination date) property. *See supra* ch. 2.

This view is supported by an analysis of the Act and the comments to UMPA. Section 766.01(10) defines *income* to mean “wages” and wage substitutes, or “economic benefits having value attributable to the effort

of a spouse” (among other items not here relevant). However, the comment to UMPA section 1 points out that the classification section classifies income earned or accrued during marriage and after the determination date as marital property; this comment clearly implies that the income, whether in the form of wages or otherwise, must first be earned or accrued to constitute marital property.

Section 766.31, which addresses the classification of spouses’ property, by its terms deals with “property.” This, of course, leads back to the definition of property in section 766.01(15). However, when section 766.31(4) specifically refers to income, it provides that “income *earned or accrued* by a spouse or attributable to property of a spouse during marriage and after the determination date is marital property.” (Emphasis added.) The UMPA section 4 comment, relating to the interest of spouses as a present equal undivided interest in marital property, states as follows:

Marital property under the Act is created *as assets are acquired* by the spouses, whether from income from the effort of either spouse during marriage, as income attributable to passive or investment sources, or as appreciation of or in an exchange for or rollover of existing marital property. When the assets are acquired from such sources, the incidents and attributes of marital property, including the creation of a present legal interest, attach simultaneously with the acquisition. The assets so acquired are instantly classified or characterized as marital property.

The UMPA section 4 comment covering transitional matters makes a similar point in discussing the “income rule” (i.e., the rule that all income from whatever source is marital, except as specifically provided): “income is marital only if ‘*earned or accrued*’ after the determination date [and] during marriage” (emphasis added). The UMPA section 4 comment refers yet again to “earned or accrued.” The “principal” of predetermination date property retains its prior classification, with the income rule affecting income earned or accrued after the determination date and during marriage by classifying it as marital property; the income “is not principal, and it is received and regulated by the Act’s provisions only when the claim of right to it occurs by virtue of its having been earned or accrued after [the determination date and during marriage].” UMPA § 4 cmt. (emphasis deleted).

It is also significant to note that neither the Act nor the comments to the management and control section of UMPA refer to future wages or, indeed, future income. However, in some instances in which there could

be doubt about the Act's treatment of these items, a specific statutory provision is included. Thus, for example, section 766.51(1)(e) provides that a spouse acting alone may manage and control "[a]ny right of an employee under a deferred employment benefit plan that *accrues* as a result of that spouse's employment" (emphasis added).

Beyond an analysis of the Act and the comments to UMPA, the experience of other community property states leads to divergent conclusions regarding the treatment of future income, based on the peculiarities of those states' constitutional, statutory, and case law. Most of the decisions relating to defining community property interests have arisen at the dissolution of the marriage. *Compare* *Speer v. Speer*, 25 Cal. Rptr. 729 (Ct. App. 1962) (characterizing future earnings as "mere expectancy") and *Jensen v. Jensen*, 665 S.W.2d 107, 109 (Tex. 1984) (holding that although spouse's time or effort "belongs" to community, there is no community property until that time or effort has produced an asset; that asset becomes community property "when received") with cases cited § 5.23, *infra*. These cases may have less relevance in determining the nature of a spouse's rights in the credit context during an ongoing marriage, particularly under the Act, given its purposes. *See infra* § 5.55.

The treatises—for example, de Funiak and Vaughn, *supra* § 5.9—do not lend significant support to a position that future wages constitute community property. For example, with reference to the Spanish roots of modern community property in the United States, de Funiak and Vaughn state that "[o]rdinarily, whatever was acquired, earned, gained or purchased by the husband and wife during the marriage [through labor and industry] belonged to both by halves." *Id.* at 140. The non-wage-earning spouse's ownership in half of the wages passed to that spouse "automatically *ipso jure* without the necessity of delivery," and did not depend on the earning spouse placing the earnings or gains in the non-wage-earning spouse's hands, but was "related . . . to the very inception of the right to such earnings and gains." *Id.* at 142. The emphasis seems to be that the equal ownership arose when the wages were "earned." *Id.* at 146.

Similarly, in discussing various employment benefits, de Funiak and Vaughn point out that in determining whether the benefits are community or separate, the status of the employee spouse "at the time the right is acquired becomes important." *Id.* at 148–49. This analysis also applies at dissolution of the marriage and in determining control of

community property. *Id.* at 152, 260. The analysis is based on what is “earned or gained” and does not support a proposition that community property exists at any earlier point.

Similar reasoning is also evident in the prefatory note to UMPA:

Some of the root concepts [of marital property] can be traced to the sharing ideal which is at the center of the historical community property approach. The fundamental principle that ownership of all of the economic rewards from the personal effort of each spouse during marriage is shared by the spouses in vested, present, and equal interests is the heart of the community property system. . . . Under [UMPA], the sharing of property is recognized by creation of a present interest simultaneously with acquisition of property by effort during marriage. The interest is legally defined and enforceable. It permeates assets *as they are acquired* and continues to permeate them as they are invested and reinvested, as they are exchanged and transferred, and as they grow or diminish.

(Emphasis added.)

Consideration of the treatment of future wages under pre-Act law in Wisconsin is not particularly helpful. Future wages have been discussed in the context of wage assignments as a matter of Wisconsin property law, but the best that can be said is that their nature is unclear. In the early case of *State ex rel. State Bank v. Hastings*, 15 Wis. 83 (1862), the court characterized future wages from existing employment as representing a “possibility coupled with an interest, and as such capable of being assigned,” based on their “potential existence.” *Id.* at 85. The court also characterized future wages as having sufficient “hope or expectation of means founded on a right *in esse*” and analogized to the “next cast of the fisherman’s net, or fruits or animals not yet in existence, or the good will of a trade.” *Id.*

On the other hand, the court in *Porte v. Chicago & Northwestern Railway Co.*, 162 Wis. 446, 156 N.W. 469 (1916), emphasized the policy consideration that wage assignments tend to subject wage earners to unreasonable conditions operating against the general welfare. The court in *Porte* held that wages relating to future employment are “a mere possibility not coupled with an interest” and accordingly are not assignable. *Id.* at 449.

In any event, it can legitimately be questioned whether Wisconsin common law is relevant in determining the nature of future wages for

purposes of management and control in a marital property context. In fact, some authors have asserted that common-law concepts should not be applied to community property. For example, one author calls it “utter folly” to attempt to “interpret community doctrine through common law eyes. One is the antithesis of the other, and the use of common law dogma to interpret community problems is a perversion of the highest order.” Vaughn, *supra* § 5.8, at 28; *see also id.* at 48–49.

An analysis of the Wisconsin statutes relating to wage assignments reveals that, as a matter of general public policy and except with respect to the support of dependents, Wisconsin discourages the assignment of future wage income. *See generally* Wis. Stat. §§ 422.404 (wage assignments with respect to credit transactions), 767.75 (assignment of income for payment obligations), 241.09 (wage assignments generally). These statutes have not been affected by the Act, although future legislation may clarify their application. *See supra* §§ 4.18, *infra* § 8.40.

### **c. Nature of Future Income in Credit Context** **[§ 5.24]**

As noted in section 5.23, *supra*, future income from personal efforts does not constitute property under the Act for property law purposes. Does such future income constitute property subject to management and control under the Act in the credit context? Decisions in other community property states may be helpful in answering this question. A broad definition of property is emerging in community property states, particularly in the divorce context, and may assist in interpreting the Wisconsin Act.

Divorce cases in several states, including both community property and common-law jurisdictions, have considered earning capacity in a broad sense to be part of the community or the marital estate. These cases have recognized the value (if not property rights) in an education, degree, or license obtained by a spouse during the marriage, as well as in the enhanced future earning capacity of both spouses as a result of an education. These considerations have been held relevant in making an equitable distribution of the marital estate.

The cases are based on a recognition that efforts during the marriage have produced something of value, akin to an asset, that can be expected to provide future returns beyond those that could or would have been

generated in its absence. See Carol S. Bruch, *The Definition and Division of Marital Property in California: Towards Parity and Simplicity*, 33 Hastings L.J. 769, 813 n.170 (1982), and cases cited therein. See also generally Joan M. Krauskopf, *Recompense for Financing Spouse's Education: Legal Protection for the Marital Investor in Human Capital*, 28 Kan. L. Rev. 379 (1980); Thomas D. Schaefer, *The Interest of the Community in a Professional Education*, 10 Cal. W. L. Rev. 590 (1974); Jon A. Chandler, *A Property Theory of Future Earning Potential in Dissolution Proceedings*, 56 Wash. L. Rev. 277 (1981); Michael G. Walsh, Annotation, *Spouse's Professional Degree or License as Marital Property for Purposes of Alimony, Support, or Property Settlement*, 4 A.L.R.4th 1294 (1981). Wisconsin decisions are consistent with this analysis in recognizing that earning capacity may be part of the marital estate. See *Haugan v. Haugan*, 117 Wis. 2d 200, 343 N.W.2d 796 (1984); *Roberto v. Brown*, 107 Wis. 2d 17, 318 N.W.2d 358 (1982); *Lundberg v. Lundberg*, 107 Wis. 2d 1, 318 N.W.2d 918 (1982). The court in *Settipalli v. Settipalli*, 2005 WI App 8, 278 Wis. 2d 339, 692 N.W.2d 279, distinguished the *Haugan* and *Lundberg* decisions by limiting the earning capacity that may be considered part of the marital estate to only that which is enhanced during the marriage, as opposed to that which is enhanced before the marriage or that which is simply *not* enhanced during the marriage.

Deferred employment benefits trigger a similar analysis in community property states in the divorce context. Even when such benefits are nonvested and depend entirely on the voluntary future actions of the divorced spouse, courts have recognized the value of these benefits and have divided the marital estate on the basis of the spouses' "property interests" in them. See *In re Marriage of Brown (Brown v. Brown)*, 544 P.2d 561 (Cal. 1976); see also William A. Reppy, Jr., *Community and Separate Interests in Pensions and Social Security Benefits After Marriage of Brown and ERISA*, 25 U.C.L.A. L. Rev. 417 (1978).

Wisconsin cases appear to be generally consistent with the above analysis of deferred employment benefits. See *Bloomer v. Bloomer*, 84 Wis. 2d 124, 267 N.W.2d 235 (1978); *Leighton v. Leighton*, 81 Wis. 2d 620, 261 N.W.2d 457 (1978); *Heatwole v. Heatwole*, 103 Wis. 2d 613, 309 N.W.2d 380 (Ct. App. 1981). However, Wisconsin courts have made it clear that any employer or employee contributions to be made to a retirement plan after a divorce are not to be considered in the division of the marital estate at divorce. *Bloomer*, 84 Wis. 2d at 127 n.1.

➤ *Comment.* It can be argued that application of the findings in the Wisconsin cases discussed above should be limited to the divorce context, in contrast to considerations that apply in an ongoing marriage or to considerations of property law issues.

A commentator on community property law has suggested that characterizing future employment (and, hence, future earnings) as a “mere expectancy” is an insufficient analysis and that a concept of an “earned expectancy” belonging to the community should be recognized. Reppy, *supra* § 5.24, at 440–42 (footnotes omitted).

In view of the nature of community property and the necessity of adapting its concepts to modern needs, some commentators and courts, especially in the divorce context, have extended the scope of community property beyond assets in hand, earned or accrued wages or income, present or future property interests, or contractual rights. For example, one commentator has stated that “[c]redit may constitute a community asset.” *Washington Community Property Deskbook* 4-23 (2d ed. 1989). Similarly, it has been suggested that “[t]he major asset of the community is the labor and industry of the spouses, and the wealth that is gained by the expenditure of this commodity, jointly or individually, is community property.” Vaughn, *supra* § 5.8, at 55.

Indeed, in many (if not most) marriages, the major resource available to the spouses for credit purposes is their labor and industry. Obtaining equal access to this resource—and hence, to future wage income—appears to be a major reason for the expanded application of management and control rights in credit transactions under section 766.51(1m) and the other unique credit provisions added by the Act to UMPA. See *supra* § 5.19, *infra* § 5.55. Accordingly, for the purposes of relying on marital property and the income stream of the spouses to obtain credit, a persuasive argument can be made that the Wisconsin Marital Property Act requires future wages to be recognized as marital property in the nature of an “earned expectancy.”

Various provisions of the Act, when read together, form a further basis for arguing that future wages are marital property. Section 766.31(4) states that when earned or accrued by a spouse or attributable to the property of a spouse, income is marital property. When earned, wages are recoverable to satisfy credit acquired in expectation of their being earned. Moreover, in addition to wages, income is defined as “economic benefits having value attributable to the effort of a spouse.”



Wis. Stat. § 766.01(10). It can be argued that the availability of credit based on future wage income (and past payment history, i.e., creditworthiness) is an economic benefit that can be used to acquire assets and that must, according to this reasoning, fall within the Act's definition of property for management purposes in the credit context.

Thus, it appears consistent with the realities and purposes of the Act to conclude that the availability of credit (i.e., creditworthiness) is a (nontitled) marital asset under the Act, subject to the management and control of either spouse, and hence usable by either spouse in obtaining credit.

#### **d. Nature of Management and Control; Purchase Money Security Interest [§ 5.25]**

The Act's management and control rights over marital property include the right to "assign, create a security interest in, mortgage, encumber . . . or otherwise deal with [marital] property as if it were property of an unmarried person." *See* Wis. Stat. § 766.01(11). Under section 766.51, the allocation of management and control rights is based on title—that is, how the asset is "held"—except as to the expanded application of management and control rights in credit transactions under section 766.51(1m). Section 766.51(1m) specifically excludes the right to manage and control the five types of business assets and "the right to assign, create a security interest in, mortgage or otherwise encumber marital property" unless the applicant spouse alone may otherwise manage and control the property. However, an applicant spouse does have the power to create a security interest in marital property in a purchase money secured transaction. A *purchase money security interest* is a security interest that is created when a buyer uses a lender's money to make a purchase and immediately gives the lender security. *Black's Law Dictionary* 1478 (Bryan A. Garner ed., 9th ed. 2009). A common example of a purchase money security interest is a home mortgage. This is because the property acquired with the credit is initially "untitled" property (not held in the name of either spouse), and section 766.51(1)(am) provides that a spouse acting alone may manage and control such property. The purchasing spouse may have the property titled solely in his or her name and may grant the security interest. *See* Wis. Stat. Ann. § 766.51(1m) Legis. Council Notes—1985 Act 37, §§ 84 to 87 (West 2009).

In sum, the Act's expanded application of management and control rights in a credit transaction by a nontitled spouse is not by itself sufficient to permit the creation of a secured interest in marital property, other than a purchase money security interest. *See supra* § 5.19, *infra* § 5.42 (concerning management and control, especially for purposes of obtaining unsecured credit); *see also infra* §§ 5.111–.135 (concerning practical considerations, especially sections 5.129–.135, *infra*, regarding Act's effect on secured credit).

#### **e. Conclusion [§ 5.26]**

Despite the fact that future income from personal efforts does not constitute property under the Act for property law purposes, in the context of obtaining credit under the Act the more persuasive view is that future wages constitute an economic benefit analogous to marital property. It appears in practice that creditors treat an anticipated future stream of marital property income as marital property for the purpose of granting credit, and this is consistent with the policy of the law.

#### **4. Future Unearned Income [§ 5.27]**

Although the discussion in sections 5.21–.25, *supra*, focuses on future *earned* income of the spouses, the issue of whether, in the credit context under the Act, property includes future *unearned* income of the spouses is essentially the same. Under the Act, unless within specific exceptions (such as, for example, the exceptions for income from trusts or income subject to a unilateral statement), income from all assets of either or both spouses (whether from marital property or nonmarital property) is classified as marital property, just as earned income is classified as marital property. *See* Wis. Stat. § 766.31(4). With respect to the proper characterization of future unearned income, the conclusions reached in sections 5.21–.25, *supra*, would similarly appear to apply to future unearned income in the credit context.

#### **D. Bona Fide Purchaser Protection [§ 5.28]**

Under the Act as well as under UMPA, a creditor dealing with a spouse or spouses having management and control rights is protected if the creditor meets the definition of a *bona fide purchaser*. *See supra*

§ 4.64. If the definition is met, any claims of the other spouse (and any claims asserted through or under the other spouse), or any objections that either of the spouses may have between themselves regarding the exercise of management and control rights, will not affect the creditor. *See* Wis. Stat. § 766.57; UMPA § 9 cmt. The intent of the Act and UMPA is to arrange spouses' property interests and management rights in such a way as to avoid disrupting commercial interests and complicating third parties' transactions with married persons. This objective is accomplished in part by insulating from marital property claims commercial interests, including creditors, who rely on title. According to one commentator, under UMPA, nondonees can safely deal with each spouse, and collection remedies of unsecured creditors are improved (although UMPA may tend to shrink the assets available to creditors of a deceased spouse who leaves a surviving spouse). *See* Wellman, *supra* § 5.5, at 718; *see also infra* § 5.102.

Under section 766.57, a secured creditor constitutes a purchaser, since section 766.57(1)(b) defines *purchase* to include the acquisition of property (which, under section 766.01(1), would include the creditor's acquisition of an interest in property) by "discount, negotiation, mortgage, pledge or lien, or otherwise [dealing] with property in a voluntary transaction other than a gift." (For purposes of the Act, the term *acquiring* includes "reducing indebtedness on encumbered property and obtaining a lien on or security interest in property." Wis. Stat. § 766.01(1).) Thus, creditors are included as purchasers as long as they give "value" for property. Wis. Stat. § 766.57(1)(a). Under the Act, a creditor (as a purchaser) gives value if the creditor acquires the property "in return for a binding commitment to extend credit, as security for or in total or partial satisfaction of a pre-existing claim, ... or, generally, in return for any consideration sufficient to support a simple contract." Wis. Stat. § 766.57(1)(c).

To constitute bona fide purchasers, creditors, as purchasers of property for value, must satisfy several conditions:

1. They must not have been "knowingly a party to fraud or illegality affecting the interest of the spouses or other parties to the transaction";
2. They must not "have notice of an adverse claim by a spouse"; and
3. They must have "acted in the transaction in good faith."

Wis. Stat. § 766.57(1)(a). For these purposes, “[a] person has notice of a fact if the person has knowledge of it, receives a notification of it, or has reason to know that it exists from the facts and circumstances known to the person.” Wis. Stat. § 766.01(13). Notice of the existence of a marital property agreement, a marriage, or a termination of a marriage (by death or by decree of dissolution) does not affect a creditor’s status as a bona fide purchaser. Wis. Stat. § 766.57(2); *see infra* § 5.36. Finally, the effect of the bona fide purchaser protection provision may not be altered by a marital property agreement. Wis. Stat. § 766.57(3).

➤ **Comment.** It is clear that the language referring to “termination” of a marriage was intended to ensure protection of bona fide purchasers who have notice of the termination of the marriage, whether by death or otherwise. Wis. Stat. Ann. § 766.57(2) Legis. Council Notes—1985 Act 37, §§ 110, 111 (West 2009).

In routine credit transactions, secured creditors will be bona fide purchasers if the property involved is marital property and the spouse involved has the right to manage and control the property. When a secured creditor acquires marital property from a spouse under those circumstances, the creditor’s acquisition is free from any claim of the other spouse. However, the status of unsecured creditors as bona fide purchasers is not as clear.

It can be argued that only a secured creditor can achieve the status of a bona fide purchaser. This may be the rule since, under section 766.57(1)(a), the term *bona fide purchaser* means one who purchases property, and under section 766.57(1)(b), the term *purchase* means “to acquire property.” An unsecured creditor does not acquire property, at least not until the unsecured creditor has obtained a judgment on the debt (and with respect to real estate, until the judgment is docketed, or with respect to personal property, until an execution is levied). In the credit context, one commentator appears to characterize bona fide purchaser protection as available only to secured creditors. *See Wellman, supra* § 5.5, at 721. On the other hand, it also can be argued that acquiring a promise from a debtor to repay a debt is sufficient to bring an unsecured creditor within the definition of *purchaser* for the purposes of the Act’s rules relating to bona fide purchasers. The latter argument seems more consistent with the purposes of the Act’s credit provisions.

## **E. Relationships Based on Categories of Obligations [§ 5.29]**

### **1. In General [§ 5.30]**

The effect of the Wisconsin Marital Property Act, together with other Wisconsin statutes and Wisconsin case law, is to create a two-element system. The first element is the personal liability of a spouse or the spouses. The second element is the Act's system of categories of obligations that determine the property that can be reached to satisfy the type of obligation involved. *See infra* § 5.32.

### **2. Family-purpose Doctrine [§ 5.31]**

Like UMPA, the Act adopts the family-purpose doctrine by providing that:

1. "An obligation incurred by a spouse during marriage, including one attributable to an act or omission during marriage, is presumed to be incurred in the interest of the marriage or the family," Wis. Stat. § 766.55(1); and
2. An obligation so incurred may be satisfied from *all* marital property, Wis. Stat. § 766.55(2).

This chapter generally refers to this rule as the *family-purpose doctrine* and to an obligation within that doctrine as a *family-purpose obligation*.

The Act's version of the family-purpose doctrine is drawn from, and is analogous to, the family-purpose doctrine in other community property states. *See supra* § 5.9. The doctrine's scope under the Act is extremely broad. The comment to UMPA section 8 indicates that the doctrine covers any contract or tort obligation having a "relation to the marriage, or the family, or the community"; this coverage is in contrast to "those obligations incurred for the purely personal purposes of an incurring spouse." UMPA § 8 cmt. According to one commentator, the exception under the family-purpose doctrine for purely personal obligations will arise "only in unusual situations of little concern to commercial interests." Wellman, *supra* § 5.5, at 745. This commentator suggests that nonfamily-purpose obligations should apply only to attempted "tort

claim collections arising from activity devoid of any marital interest.” *Id.* at 747.

The family-purpose doctrine is further buttressed by the presumption under the Act that an obligation incurred by a spouse is within the doctrine’s scope. *See* Wis. Stat. § 766.55(1). The burden is on the party asserting that the obligation is not within the family-purpose doctrine to establish that this fact is more probable than not. *See* Wis. Stat. § 903.01. In addition, in connection with family-purpose obligations, the presumption can be made irrebuttable (other than as to remedies between the spouses) if, at or before the time the obligation is incurred, a separately signed statement of family purpose is given to the creditor by the obligated or incurring spouse. Wis. Stat. § 766.55(1). Such a separate statement is included in most credit applications.

Since UMPA borrowed the family-purpose doctrine from the community property states that rely on it, case law in those states is relevant to an appreciation of the doctrine’s very broad scope. For example, under Washington’s version of the family-purpose doctrine, the presumption of a community debt seems to apply even if the funds are subsequently used for a purpose that does not benefit the spouses or family. These rules “so favor the creation of community debts, that, if the court can find merely a community property benefit, it will find community liability.” Todd M. Johnson, *Limitations on Creditors’ Rights to Require Spouses’ Signatures Under the ECOA and Washington Community Property Law*, 4 U. Puget Sound L. Rev. 333, 342 (1981).

### **3. Categories of Obligations [§ 5.32]**

To determine what property is available to creditors to satisfy obligations after the spouses’ determination date, it is necessary to categorize the obligations in question. *See infra* ch. 6. The following table summarizes the categories of obligations, the personal liability of the spouse or spouses, and the property available to satisfy each category of obligation.

Categories of Obligations	Personal Liability	Property Available to Satisfy Obligation
Support of the other spouse or a child of the marriage § 766.55(2)(a)	Each spouse <sup>1</sup>	All marital property and all other property of obligated spouse
An obligation incurred in the interest of the marriage or family § 766.55(2)(b)	Incurring spouse	All marital property and all other property of incurring spouse <sup>2</sup>
An obligation arising before marriage (or, for spouses married before 1/1/86, a pre-Act obligation) § 766.55(2)(c)	Incurring spouse	Incurring spouse's nonmarital property and that part of marital property that would have been incurring spouse's property but for marriage (or but for enactment of Act, as case may be) <sup>3</sup>
Liability of a spouse arising from a tort committed by that spouse during marriage § 766.55(2)(cm)	Tortfeasor spouse	Tortfeasor spouse's nonmarital property and that spouse's one-half interest in marital property
Any other obligation a spouse incurs during marriage, including obligations that are not in the interest of the marriage or the family <sup>4</sup> § 766.55(2)(d)	Incurring spouse	Incurring spouse's nonmarital property and that spouse's one-half interest in marital property, in that order <sup>5</sup>

<sup>1</sup> Wis. Stat. §§ 49.90(1m), 765.001(2); *see infra* §§ 5.105–.110 (extent of duty of support and doctrine of necessities).

<sup>2</sup> Accordingly, if the obligation was incurred in the interest of the marriage or the family, the creditor is able to reach assets beyond those held by the incurring spouse and beyond those over which the incurring spouse has rights of management and control.

<sup>3</sup> Regarding rights of reimbursement, see chapter 8, *infra*.

<sup>4</sup> *See supra* § 5.31 (broad scope of family-purpose doctrine and hence narrow scope of excluded obligations).

<sup>5</sup> This is the only category in which there is an order-of-satisfaction requirement. Regarding rights of reimbursement, see chapter 8, *infra*.

The Act (including the provisions in the above table) applies to spouses after their determination date, *see* Wis. Stat. § 766.55(2), but only “during marriage.” As defined by the Act, the term *during marriage* means “a period in which both spouses are domiciled in this state,” which begins at their determination date and which ends at (1) the dissolution of the marriage, (2) the death of one of the spouses, or (3) the date when one of the spouses ceases to be domiciled in Wisconsin. Wis. Stat. § 766.01(8).

➤ **Note.** In view of the definition of the term during marriage under section 766.01(8), there appears to be a gap in section 766.55(2), in that the section does not specify the property available to a creditor to satisfy an obligation incurred by a spouse after 1985 while the spouses are married but during a period when one or both of the spouses are not domiciled in Wisconsin. For a discussion of such obligations, *see* sections 5.137 and 6.30, *infra*.

With respect to tort obligations, in view of the completeness of the coverage of torts under section 766.55(2)(cm) and the fact that only one-half of marital property may be reached to satisfy a spouse’s liability arising from a tort committed by that spouse during marriage, it appears that the family-purpose doctrine has no application to tort liabilities. Hence, there appears to be no distinction under the Act between family-purpose torts and nonfamily-purpose torts; it appears that all torts committed by a spouse during marriage are fully covered by section 766.55(2)(cm) and do not fall within section 766.55(2)(d) (covering any other obligation incurred by a spouse during marriage). *See infra* §§ 6.27, 12.106.

## **F. Additional Special Rules [§ 5.33]**

### **1. In General [§ 5.34]**

The Act contains additional special rules that apply to creditor-debtor relationships. These rules relate to the Act’s attempt to protect creditors with respect to predetermination date obligations; the effects of marital property agreements, unilateral statements (as to income on nonmarital property), and decrees; the effects of the termination of the marriage by dissolution or death; and the effects of a change in domicile. Also, the Act does not affect exemptions otherwise provided in the law or certain



provisions of chapter 706 with respect to real estate. These special rules are summarized below.

## **2. Predetermination Date Obligations [§ 5.35]**

Section 766.55(3) addresses predetermination date obligations. This section provides that the Act does not “alter the relationship between spouses and their creditors with respect to any property or obligation in existence on the determination date.” *See supra* § 2.8 (definition of *determination date* under Act). Presumably, to the extent that significant modifications are made in contractual relationships after the determination date, the provisions of the Act would apply.

As a practical matter, however, the operation of the Act may adversely affect the collection rights of a predetermination date creditor of one spouse. This could occur as a result of the other spouse’s ability (after the determination date) to incur obligations that can be satisfied from marital property, including wages on which the predetermination date creditor may have relied. *See infra* § 5.138. Similarly, in extending credit to one spouse after the determination date (particularly when reliance is placed on marital property, including wages of the other spouse), creditors will need to consider predetermination date obligations of the other spouse that can be satisfied from marital property, including wages of the other spouse.

## **3. Marital Property Agreements, Unilateral Statements, and Decrees [§ 5.36]**

A provision of a marital property agreement does not affect the relationship between a creditor and a married person unless the creditor consents or has actual knowledge of the provision when the obligation was incurred (or is furnished a copy of the agreement under certain circumstances). The following provisions of the Act are relevant with respect to the effects of marital property agreements on creditors.

1. Section 766.55(4m) provides that “[e]xcept as provided under [section] 766.56(2)(c), no provision of a marital property agreement or of a decree under [section] 766.70 [, which concerns spousal remedies,] adversely affects the interest of a creditor unless the creditor had actual knowledge of that provision when the obligation

to that creditor was incurred” (or, regarding open-end plans, when the plan was entered into). The statute also provides that this statutory protection may not be altered by such an agreement or decree. This protection for the creditor extends to any subsequent renewal, extension, modification, or use of the obligation or open-end plan.

➤ **Note.** If a copy of the document is furnished to the creditor before credit is granted, the creditor is bound by the document’s provisions even without actual knowledge. *See* Wis. Stat. § 766.56(2)(c).

➤ **Comment.** It is unclear how much information, short of a copy of the complete document, must be given to the creditor for that creditor to have actual knowledge under section 766.55(4m). For instance, it is not clear if a letter alerting the creditor to the existence of the agreement and the nature of the provision would suffice. *See infra* § 5.64.

Section 766.55(4m) specifically states that it does not affect the application of chapter 706 regarding the effect of recording interests in real property. Accordingly, the recording of a marital property agreement does not constitute actual or constructive notice of any of its provisions, except as the marital property agreement may affect specific parcels of real estate referred to in the agreement and such other matters as are governed by chapter 706.

2. Section 766.56(2)(a) provides that recording a marital property agreement (or unilateral statement regarding income on nonmarital property) does not provide third parties (including creditors) actual or constructive notice of the agreement. Again, however, the provisions of this paragraph are subject to the application of chapter 706 regarding the effect of recording interests in real property.
3. Section 766.56(2)(b) provides that creditors in credit transactions under the Wisconsin Consumer Act, Wis. Stat. chs. 421–427 (hereinafter the Wisconsin Consumer Act or the Consumer Act), are to include in written credit applications a notice stating the lack of effect on the creditor of a marital property agreement, unilateral statement as to income on nonmarital property (under section 766.59), or court decree (under section 766.70) unless the creditor,

before the credit is granted, is furnished a copy of the agreement, statement, or decree, or has actual knowledge of the adverse provision in the agreement.

If the applicant spouse in any credit transaction (whether or not governed by the Consumer Act) discloses the existence of a marital property agreement and provides a copy of it to the creditor before credit is granted or before an open-end plan is entered into, “the creditor is bound by any property classification, characterization of an obligation, or management and control right contained in the agreement or decree.” Wis. Stat. § 766.56(2)(c); *see also infra* § 5.51 (applicability of section 766.56(2)(b) and (c)).

These sections, when applicable, apparently control at the time a spouse applies for credit; they seem to override the general provision in section 766.57(2), which provides that “[n]otice of the existence of a marital property agreement . . . does not affect the status of a purchaser as a bona fide purchaser.”

➤ **Query.** When section 766.56 applies, what is the effect, other than the \$25 penalty provided in section 766.56(4)(b), if a Consumer Act creditor fails to include the required notice under section 766.56(2)(b) in the written credit application? Is the creditor bound by adverse provisions contained in a marital property agreement of which the creditor is not aware? It would appear not, since this result would be inconsistent with the “actual knowledge” requirement of section 766.55(4m) or the copy provisions of section 766.56(2)(c). *See Park Bank-West v. Mueller*, 151 Wis. 2d 476, 444 N.W.2d 754 (Ct. App. 1989) (creditor’s failure to give notice to nonapplicant spouse under section 766.56(3)(b) resulted only in statutory \$25 penalty); *see also infra* § 5.70 (discussing *Park Bank-West*).

There seems to be no penalty imposed on an applicant spouse vis-à-vis the applicant’s creditor if the applicant, when asked, does not provide a copy of the agreement. The nonapplicant spouse may have a remedy, however, against the applicant spouse who failed to provide the copy. *See* Wis. Stat. § 766.70(1); *see also infra* § 8.18.

➤ **Practice Tip.** A practical problem arises for a creditor when the applicant spouse furnishes a copy of the marital property

agreement, thereby binding the creditor by its provisions. Since the provisions of the marital property agreement may be unclear, and professional help may be required to interpret them, a creditor may be justified in charging a fee to cover the cost of obtaining a professional opinion concerning the agreement.

4. Section 766.55(4) provides that a written consent signed by a creditor that diminishes the creditor's rights with respect to the satisfaction of obligations is binding on the creditor.

#### **4. Dissolution of Marriage [§ 5.37]**

The dissolution of a marriage may affect the rights of creditors. A *dissolution* is defined as a termination of a marriage by decree of dissolution, divorce, annulment, declaration of invalidity, legal separation, or separate maintenance. Wis. Stat. § 766.01(7). Termination of a marriage by death is not included in the definition of dissolution. *See* Wis. Stat. §§ 766.55(8), 859.18(6); *see also infra* § 5.99.

Under section 766.55(2m), in the event of a dissolution, *unless* the decree or any amendment to the decree provides otherwise, “no income of a nonincurring spouse is available for satisfaction of an obligation [incurred by a spouse in the interest of the marriage or family] after entry of the decree.” However, marital property assigned to a spouse under the decree is available to satisfy an obligation incurred in the interest of the marriage or family, up to the value (as of the date of the decree) of the marital property so assigned. Further, if the decree provides that the nonincurring spouse is responsible for satisfaction of the obligation, it may be satisfied as if both spouses had originally incurred it. Wis. Stat. § 766.55(2m).

The clear import of section 766.55(2m) is that the decree may provide that future income of the nonincurring spouse must be made available to satisfy an obligation incurred within the family-purpose doctrine during the marriage, regardless of personal liability. In addition, future income or assets of the nonincurring spouse are available, regardless of the divorce, to satisfy an obligation arising from the duty of support or under the necessities doctrine. *See St. Mary's Hosp. Med. Ctr. v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 206 (Ct. App. 1994) (discussed at sections 5.106 and 5.110, *infra*); *see also infra* § 5.98 (practical problems for creditors).

## 5. Change in Domicile [§ 5.38]

As noted in section 5.32, *supra*, the existence of marital property under the Act depends on both spouses' being domiciled in Wisconsin. Thus, a change in domicile to another state by one or both spouses may affect the accrual of additional marital property after the date of the change. *See* Wis. Stat. §§ 766.01(5)(b), (8), .03; *see also supra* § 2.8. Although the change in domicile of either spouse or both spouses would not affect marital property assets owned by both spouses at the time of the change, it might affect the nature of the income from the asset. *See infra* ch. 13. This creates practical problems for creditors. *See infra* § 5.100.

➤ **Historical Note.** As originally enacted, the Marital Property Act required that spouses have their “marital domicile” in Wisconsin in order for the Act to apply. The 1988 Trailer Bill eliminated the concept of *marital domicile* effective May 3, 1988. As a result, the Act applies only while both spouses are domiciled in Wisconsin.

## 6. Exemptions [§ 5.39]

Section 766.55(5) states that the Act does not affect any exemptions, as provided by any other law, of any property of spouses from availability for satisfaction of an obligation. *See* Wis. Stat. §§ 425.106 (property exempt under Wisconsin Consumer Act), 815.18 (property exempt generally), .20 (homestead exemption); *see also infra* § 6.68.

## G. Conclusion: Means for Obtaining and Extending Credit [§ 5.40]

Under the Act, as in the past, a spouse can use his or her nonmarital property (individual property or other, i.e., predetermination date, property) to obtain unsecured and secured credit. A creditor may reach such property based on the personal liability of the incurring spouse and any security interest granted. *See supra* § 5.32. In addition to incurring a personal obligation as a basis for obtaining credit, under the Act a spouse may use marital property over which he or she has normal (i.e., title-based) or expanded (i.e., section 766.51(1m)) management and control rights as a basis for obtaining unsecured credit. The Act also

enables a spouse having normal management and control rights over marital property to grant a creditor a security interest in that property.

If the credit will be used for a family purpose, *see supra* § 5.31, the applicant spouse may obtain credit by attribution of creditworthiness under section 766.56(1). *See infra* §§ 5.52–.55. If a family-purpose obligation is involved, the creditor may reach all nonexempt marital property assets, even those marital property assets over which the incurring spouse has no normal or expanded management and control rights. These assets would include, for example, marital property assets held by the spouses in the conjunctive (“and”) form, marital property assets held solely by the nonincurring spouse, the homestead, and the wages or other income of the nonincurring spouse. Further, under the necessities doctrine, the nonincurring spouse may be personally liable as well, in which case the creditor also may be able to reach his or her nonmarital property assets. *See infra* §§ 5.109–.110.

#### **IV. Expanded Application of Management and Control and Attribution of Creditworthiness in Credit Transactions [§ 5.41]**

##### **A. In General [§ 5.42]**

The Wisconsin Marital Property Act expands the application of management and control rights in credit transactions with married persons. *See* Wis. Stat. § 766.51(1m). This expanded application is in addition to the rights of management and control that normally apply under the Act in all relationships and transactions with married persons, including creditor-debtor relationships and transactions. *See supra* §§ 5.12–.40. Further, in credit transactions with married persons, specific provisions of the Act define duties, responsibilities, and consequences pertaining to granting and obtaining credit. These provisions, together with adoption of the family-purpose doctrine, were designed to provide each spouse full and equal access to credit based on marital property, including the income stream (i.e., wages or income from assets) of either or both spouses. *See supra* § 5.19, *infra* § 5.53.

For the purpose of obtaining credit involving a family-purpose obligation, section 766.51(1m) provides that a spouse acting alone may manage and control (but, by its terms, not encumber) all marital property

except those items of marital business property for which the “add-a-name” remedy is not available under section 766.70(3)(a)–(d) (unless that spouse may otherwise manage and control such property under the normal management and control rules). *See supra* § 5.25 (effect of section 766.51(1m) in purchase money secured transaction), *infra* §§ 8.24–.27 (add-a-name remedy and its exceptions). Briefly, these management and control exceptions are the following:

1. A partnership interest or interest in a joint venture held by the other spouse as a general partner or as a participant;
2. An interest in a professional corporation or association or similar entity held by the other spouse as a stockholder or member;
3. An asset of an unincorporated business if the other spouse is the only spouse involved in the business;
4. The stock of a nonpublicly traded corporation, as defined in section 766.70(3)(d); and
5. An interest in a limited liability company held by the other spouse as a member.

These exceptions were made to allow spouses who are actively engaged in businesses or professional enterprises to have sole management of these activities. The exceptions to the add-a-name remedy under the Wisconsin Act are broader than those under UMPA, which does not contain the second and fifth exceptions listed above.

It appears that the primary reason for the expanded application of management and control rights in family-purpose credit transactions was to trigger application of the Equal Credit Opportunity Act (ECOA), *see infra* §§ 5.77–.86, particularly Regulation B, which was promulgated by the Board of Governors of the Federal Reserve System to implement the ECOA. *See* Wis. Stat. Ann. § 766.51(1m) Legis. Council Notes—1985 Act 37, §§ 84 to 87 (West 2009); *see also infra* § 5.89. In fact, some people argue that the expanded application of management and control rights in family-purpose credit transactions, as provided in section 766.51(1m), has no significance in actual practice and that the triggering of Regulation B is the only reason for the section.

Some creditors in Wisconsin have argued that, although they are legally required to rely on the credit applicant spouse's management rights over marital property assets held by the other spouse as well as the income of the other spouse, the applicant spouse often lacks practical control over such assets or income and therefore has no real ability to apply them to repay the debt incurred. *See infra* §§ 5.97–.104. These creditors argue that they should not be forced to consider marital property to which the applicant spouse lacks effective access, and therefore, before granting the credit, they should be allowed to require the signature of the other spouse since the applicant spouse may not have access to that marital property. *See infra* § 5.102.

Under the Act, however, statutory remedies are provided to promote effectiveness of the nontitled spouse's rights of management and control. Without these remedies, it could be argued that section 766.51(1m) lacks sufficient substance to support access to credit. Among other remedies, a spouse may bring a court action to obtain an accounting of the other spouse's property and obligations. *See* Wis. Stat. § 766.70(2). More importantly, perhaps, the court can determine the classification of property and order access to marital property. *Id.* Also, under the previously mentioned add-a-name remedy, the court may order the name of a spouse added to a document evidencing ownership of marital property held in the name of the other spouse alone (except for the five excluded types of business assets). *See* Wis. Stat. § 766.70(3). Finally, under certain circumstances, the court may order limitations on the other spouse's management and control rights, including rights with respect to property to be received in the future. *See* Wis. Stat. § 766.70(4). An action based on a violation of the good-faith duty might also be available, for example, if the other spouse is using his or her rights of management and control to frustrate the applicant spouse's exercise of his or her rights in obtaining credit (e.g., by obtaining lines of credit beyond his or her reasonable needs, thereby reducing the amount of credit available to the other spouse). *See* Wis. Stat. §§ 766.15, .70(1); *see also infra* ch. 8.

Probably more important from a practical viewpoint, to promote expanded access to credit for the nonpropertied (or less propertied) or nonwage-earning (or lower-wage-earning) spouse, when a family-purpose obligation is being incurred, the Act requires a creditor to consider *all* available marital property in deciding whether to grant credit and the extent and terms of the credit. *See* Wis. Stat. § 766.56(1); *see infra* § 5.55. It should be noted that with respect to an obligation



incurred in the interest of the marriage or family, the five types of assets excepted from the management and control rules under section 766.51(1m)(b) are not included in the assets that the creditor must consider and may reach to satisfy the obligation. *See* Wis. Stat. §§ 766.56(1), .55(2)(b).

Further, the 1985 Trailer Bill amendment to section 766.55(1) removed the prior concern of creditors that, although the creditor was required to consider all marital property, the creditor would be foreclosed from reaching marital property if the incurring spouse, or the spouses, could convince a court that the obligation was not incurred in the interest of the marriage or the family. Section 766.55(1), as amended by the Trailer Bill, provides that a statement separately signed by the obligated or incurring spouse at or before the time the obligation is incurred, reciting that the obligation is or will be in the interest of the marriage or the family, is conclusive evidence of that fact. Pursuant to the statute, the statement does not, however, affect any right or remedy as between the spouses themselves.

## **B. Definitions [§ 5.43]**

### **1. In General [§ 5.44]**

As outlined in section 5.42, *supra*, when a spouse applies for credit that will result in a family-purpose obligation, in addition to considering the applicant spouse's creditworthiness (based on that spouse's personal liability, individual property, and predetermination date property), the creditor is required to consider all marital property available to satisfy the obligation. In considering these rules, it is necessary to clarify some definitions and to understand the purpose of the Act.

### **2. Definitions of Credit and Creditor Under Marital Property Act and Their Application [§ 5.45]**

#### **a. In General [§ 5.46]**

Application of the special provisions of the Act governing the obtaining and granting of credit requires definitions of the terms credit and creditor. The special provisions subject to these definitions include:

1. Subsections relating to the categories of obligations on the basis of which classes of assets may be reached by creditors, *see* Wis. Stat. § 766.55;
2. The expanded application of management and control rights in credit transactions, *see* Wis. Stat. § 766.51(1m); and
3. The procedures for credit transactions with married persons, *see* Wis. Stat. §§ 766.555, .56.

The interplay between the Act's definitions of credit and creditor under section 766.01(2m) and (2r) and the special provisions of the Act governing the obtaining and granting of credit produces differing applications of the special provisions.

The basic definition of the term *credit* is in section 766.01(2m)(a). That section provides that, subject to stated exceptions, “credit” means “the right granted by a creditor to defer payment of a debt, incur debt and defer its payment or purchase property or services and defer payment for the property or services.” Wis. Stat. § 766.01(2m)(a).

The basic definition of the term *creditor* is in section 766.01(2r)(a). That section provides that, subject to stated exceptions, “creditor” means “a person that *regularly* extends credit.” Wis. Stat. § 766.01(2r)(a) (emphasis added).

Sections 5.47–.50, *infra*, summarize the application of these definitions and their exceptions to the special provisions of the Act governing the obtaining and granting of credit. However, it is important to keep in mind the blanket rule that if a Wisconsin Consumer Act transaction is involved, the Consumer Act's definitions apply. Wis. Stat. § 766.01(2m)(b), (2r)(b).

## **b. Relationships Between Spouses and Creditors**

### **[§ 5.47]**

The basic definition of creditor as “a person that regularly extends credit” does not apply to subsections 766.55(3)–(4m), because of the exception to the definition contained in section 766.01(2r)(c). Hence, all creditors, whether they are incidental creditors or creditors who regularly extend credit, are subject to:

1. The provision in section 766.55(3) that chapter 766 does not alter the relationship between spouses and their predetermination date creditors (with respect to property or obligations existing on the determination date);
2. The provision in section 766.55(4) concerning the effect of a written consent signed by a creditor that diminishes the creditor's rights; and
3. The provisions in section 766.55(4m) concerning the effect on creditors of marital property agreements or decrees.

*See also* Wis. Stat. Ann. § 766.01 Legis. Council Notes—1985 Act 37, §§ 69–73 (West 2009) (stating that, regarding provisions to which the defined terms do not apply, “the terms are used in a broad sense and applying the defined terms to those provisions may inappropriately limit the provisions’ scope”).

### **c. Expanded Application of Management and Control Rights [§ 5.48]**

The basic definition of credit under section 766.01(2m) applies to the expanded concept of management and control under section 766.51(1m) for the purposes of obtaining an extension of credit for a family-purpose obligation. Since the definition of the word credit uses the word creditor, which is defined as “a person that regularly extends credit,” and since section 766.51(1m) is not included among the exceptions to the definition in section 766.01(2m)(c) and (2r)(c), the expanded management concept applies only to creditors who regularly extend credit.

### **d. Credit Procedures [§ 5.49]**

With respect to the requirement for evaluating creditworthiness in credit transactions under section 766.56(1), the basic definitions of credit and creditor apply. *See* Wis. Stat. § 766.01(2m)(c), (2r)(c) (not listing section 766.56(1) among exceptions to definitions of credit and creditor). Hence, the requirement applies only to creditors who regularly extend credit and not to incidental creditors. *See* Wis. Stat. § 766.01(2r)(a) (defining creditor to mean “a person that regularly extends credit”).

By contrast, the basic definitions of credit and creditor do *not* apply to section 766.56(2)(c) (establishing the binding effect on a creditor in a credit transaction of an applicant's disclosure of the existence of, or provision of a copy of, a marital property agreement or decree) or section 766.56(2)(d) (relating to inquiries by a creditor as to an applicant's marital status). *See* Wis. Stat. § 766.01(2m)(c), (2r)(c) (listing section 766.56(2)(c) and (d) among exceptions to definitions of credit and creditor). Accordingly, the rules of these sections apply to all types of credit transactions, regardless of whether the creditor regularly extends credit. *See* Wis. Stat. § 766.01(2r)(a) (defining creditor to mean "a person that regularly extends credit").

#### **e. Predetermination Date Open-end Plans** **[§ 5.50]**

The basic definitions of credit and creditor apply to section 766.555, which specifically deals with open-end plans that exist on the spouses' determination date but that were entered into by only one spouse. *See* Wis. Stat. § 766.01(2m)(c), (2r)(c) (not listing section 766.555 among exceptions to definitions of credit and creditor). Hence, section 766.555 applies only to creditors who regularly extend credit. *See* Wis. Stat. § 766.01(2r)(a) (defining creditor to mean "a person that regularly extends credit"). By contrast, the notice provisions of section 766.56(3)(b), which apply to postdetermination date open-end credit plans (and credit other than open-end credit), use the credit and creditor definitions of the Wisconsin Consumer Act, because the notice requirements of that section apply only to credit transactions governed by the Consumer Act. *See* Wis. Stat. §§ 766.56(3)(b), .01(2m)(b), (2r)(b).

### **3. Definitions of Credit and Creditor Under Wisconsin Consumer Act and Their Application** **[§ 5.51]**

All creditors ("persons that regularly extend credit") may be subject to civil suit for failure to properly evaluate creditworthiness under section 766.56(1). As noted in sections 5.45–.50, *supra*, the Act's definitions of credit and creditor provide that if the terms are used in connection with a transaction governed by the Wisconsin Consumer Act, they have the meanings specified in the Consumer Act. Wis. Stat.

§ 766.01(2m)(b), (2r)(b). To understand the application of the Consumer Act, it is critical to note the specific exclusions to its application contained in section 421.202. For purposes of applying the Marital Property Act, the most significant of these is the exclusion of “consumer credit transactions in which the amount financed exceeds \$25,000 . . . or other consumer transactions in which the cash price exceeds \$25,000.” Wis. Stat. § 421.202(6).

Under the Wisconsin Consumer Act, the term *credit* is defined as “the right granted by a creditor to a customer to defer payment of debt, to incur debt and defer its payment or to purchase goods, services or interests in land on a time price basis.” Wis. Stat. § 421.301(14). The Consumer Act defines the term *creditor* as a “merchant who regularly engages in consumer credit transactions or in arranging for the extension of consumer credit by or procuring consumer credit from 3rd persons.” Wis. Stat. § 421.301(16). A *consumer credit transaction* means a “consumer transaction between a merchant and a customer in which real or personal property, services or money is acquired on credit.” Wis. Stat. § 421.301(10). A *customer* is defined as a person (other than an organization) “who seeks or acquires real or personal property, services, money or credit for personal, family or household purposes, or, for purposes of ch. 427 only, for agricultural purposes.” Wis. Stat. § 421.301(17).

With respect to violations based on a creditor’s failure to attribute creditworthiness under section 766.56(1), penalties are imposed only on a “financial organization or any other credit-granting commercial institution.” Wis. Stat. § 766.56(4)(a). This is accomplished by incorporating section 138.20 into section 766.56(4)(a). The result is the imposition of penalties on a narrower class of creditors than the class of creditors that meets the basic definition of creditor under the Marital Property Act.

With respect to violations of the notice provisions of section 766.56(2)(b) and (3), this section applies only to creditors who regularly engage in Consumer Act transactions, and hence, only such creditors are subject to the \$25 liability of section 766.56(4)(b). However, although only financial organizations or other credit-granting commercial institutions may be subject to penalties under section 766.56(4)(a), and only Wisconsin Consumer Act creditors may be required to pay the \$25 liability under section 766.56(4)(b), by the terms of section 766.56(1), all “creditors” (by reference to the basic definition of creditors as “persons

that regularly extend credit”) are subject to that section’s requirements of attribution of creditworthiness.

Further, virtually all credit grantors are subject to the ECOA. *See infra* §§ 5.57 (failure to satisfy requirements of section 766.56), 5.77–.86 (ECOA). For a discussion of procedural requirements in actions alleging violations of the ECOA, see *Bolduc v. Beal Bank, SSB*, 994 F. Supp. 82 (D.N.H. 1998).

## **C. Attribution of Creditworthiness [§ 5.52]**

### **1. In General [§ 5.53]**

When a spouse applies for credit that will result in a family-purpose obligation, section 766.56(1) requires the creditor, “in evaluating the spouse’s creditworthiness,” to consider all marital property of the spouses available to satisfy the obligation. Section 766.56(1) further requires the creditor to consider the spouse’s creditworthiness in the same manner that the creditor, “in evaluating the creditworthiness of an unmarried credit applicant,” considers the property of that applicant that will be available to satisfy the obligation. In other words, all the marital property is attributed to the applicant spouse as if the applicant spouse were the sole owner (as would be the case with all property of an unmarried applicant). Thus, it is necessary to examine the nature of creditworthiness and the extent of the assets that the creditor must consider.

### **2. Definition of Creditworthiness [§ 5.54]**

The Wisconsin Marital Property Act does not define *creditworthiness*, and the word is not a defined term in any other Wisconsin statute, in the ECOA, or in Regulation B interpreting the ECOA. *See infra* §§ 5.76–.96. However, in its consideration of the ECOA, Congress used definitions similar to the following: “Generally [creditworthiness is] considered to be a function of both the applicant’s willingness and ability to pay the debt and the creditor’s rights and remedies with respect to property available for debt payment.” Ralph C. Clontz, Jr., *Equal Credit Opportunity Manual* 1-19 (3d ed. 1979 & Cum. Supp. No. 2 1984). The Senate report by the Committee on Banking, Housing and Urban Affairs (accompanying the amendment to the Truth-in-Lending Act that adopted

the ECOA) refers to a person being creditworthy “by virtue of willingness and ability to repay any obligations.” S. Rep. No. 93-278 (1974).

➤ **Note.** In assessing the creditworthiness of a person who applies for credit in a community property state, a creditor may assume that the applicant is a resident of the state unless the applicant indicates otherwise. 12 C.F.R. pt. 202, Supp. I cmt. 7(d)(3)-1.

Thus, normally a creditor’s evaluation of creditworthiness involves a two-pronged test:

1. The creditor must consider an applicant’s willingness and ability to repay the debt; this may be measured by such factors as the applicant’s payment history, employment status, expected duration of employment, and control over assets. However, this prong of the test might not be appropriate under the Act since a nontitled, nonwage-earning spouse may not have the practical ability to pay the debt.
2. The creditor must consider the assets or income stream that may be reached to satisfy the debt in the event of a default. It is on this prong of the test that the Act relies.

➤ **Comment.** The analysis of the nature of creditworthiness also demonstrates an inconsistency under the Act between what the unsecured creditor is required to consider in granting credit and what the debtor, as a practical matter, can reach to pay the debt voluntarily. In fact, the unsecured creditor is forced to take additional risks that would not exist if that creditor were dealing with an unmarried applicant and were considering that applicant’s property. These include risks of divorce, change of marital domicile with a resultant change in property rights with respect to income, and future credit actions of the nonapplicant spouse and of the nonapplicant spouse’s creditors. *See infra* §§ 5.97–.104.

### **3. Assets to Be Considered [§ 5.55]**

When a family-purpose obligation is being incurred, the only assets a creditor may exclude under section 766.56(1) in evaluating creditworthiness are the nonapplicant spouse’s individual property and

predetermination date property. The five excepted items of marital business property under section 766.70(3)(a)–(d) are not included in the property to be considered. The homestead is included in the property to be considered. The example below illustrates the application of section 766.56(1).

➤ **Example.** Assume that, before the effective date of the Act, a wife's creditworthiness would have supported credit of \$5,000 on the basis of her income stream (represented by her wage income). After the effective date of the Act, the purpose and effect of section 766.56(1) is to enable the husband, the nonwage-earning spouse, acting alone, to obtain credit up to this amount. (This assumes that the wife has not fully used this credit and that the husband's creditworthiness does not adversely affect the total credit available to the spouses.) Section 766.56(1) requires that, when the husband applies for credit, the creditor must evaluate his creditworthiness as if the wages were his.

The actions and creditworthiness of one spouse may affect the creditworthiness of the other spouse. Since the credit grantor must consider all marital property, all obligations that might affect the marital property also are relevant to the consideration of creditworthiness (as would be the case if the wages were the wages of the applicant spouse).

It appears that future income, including future wage income of the nonapplicant spouse, must be considered by the creditor. *See supra* §§ 5.21–.24. Also, it appears that future income on the nonapplicant spouse's individual or predetermination date property must be considered by the creditor, *see supra* § 5.25, since, at a minimum, it will become marital property when received, unless a marital property agreement (that has been made binding on the creditor) classifies that income as the nonapplicant spouse's individual property, or unless the nonapplicant spouse has executed a unilateral statement under section 766.59 (that has been made binding on the creditor) designating income on nonmarital property as individual property.



## **D. Penalties; Rule-Making Authority [§ 5.56]**

### **1. Violation of Marital Property Act [§ 5.57]**

A creditor that is a “financial institution or any other credit-granting commercial institution” and that violates the attribution-of-creditworthiness responsibilities under section 766.56(1), *see supra* §§ 5.52–.55, is subject to the penalties provided in section 138.20. *See* Wis. Stat. § 766.56(4)(a). Section 138.20 provides that no financial organization, as defined under sections 71.04(8)(a) and 71.25(10)(a), or any other credit-granting commercial institution may discriminate on the basis of the applicant’s sex or marital status (or other prohibited bases) in granting or extending credit. The penalty for violating section 138.20, and, hence, section 766.56(1), is \$1,000, and a separate violation arises for each individual who is discriminated against.

### **2. Violation of Division of Banking Rules Under Wisconsin Consumer Act [§ 5.58]**

Section 426.108 grants the Wisconsin Division of Banking the authority to promulgate rules prohibiting as unconscionable specific conduct in consumer-credit transactions subject to the Wisconsin Consumer Act. Pursuant to this section, the division has adopted rules with respect to discrimination on the basis of sex or marital status in connection with the granting or extending of credit. These rules are similar to the requirements under the ECOA. *See infra* §§ 5.78–.86.

The Division of Banking rules declare it to be Wisconsin policy that “no person shall be discriminated against in the granting or extension of any form of credit, or in the capacity or privilege of obtaining any form of credit,” on a prohibited basis, such as on the basis of the applicant’s sex or marital status. Wis. Admin. Code § DFI-WCA 1.85(1). Such discrimination is unconscionable conduct under section 426.108 and can therefore be the subject of injunctive relief, class actions, damages, and recovery of attorney fees under sections 426.109 and 426.110. This rule applies to merchants as defined in the Consumer Act; it does not apply, however, to “merchants chartered by any Wisconsin administrative agency which issues a regulation prohibiting discrimination in the granting of consumer credit on the basis of sex or marital status.” *Id.*

Discrimination under this rule is defined to mean, among other things, a denial of credit or an increase in the charge for credit based on the customer's sex or marital status. Discrimination includes requiring a spouse to co-sign credit documents, unless such a signature is required by statute or "is imposed without regard to sex or marital status on all similarly qualified customers who apply for a similar type and amount of credit." Wis. Admin. Code § DFI-WCA 1.85(2)(d). An exception is made when it is necessary with respect to secured credit to create a valid lien, as long as the merchant's standards of creditworthiness require the signature without regard to sex or marital status. *Id.*

► **Note.** The questions that can arise under these rules as a result of the Act are basically similar to the questions that arise under the ECOA. *See infra* §§ 5.88, .91–.96.

### **3. Rulemaking Authority [§ 5.59]**

Because of the interrelationships between the credit provisions of the Wisconsin Marital Property Act and the provisions of the Wisconsin Consumer Act, and the need to accommodate the sometimes differing purposes of the two acts, the 1985 Trailer Bill added section 766.565. *See* Wis. Stat. Ann. § 766.565 Legis. Council Notes—1985 Act 37, § 109 (West 2009). Under section 766.565(7), the Division of Banking is authorized to promulgate rules to interpret chapter 766 and the Consumer Act, "consistent with [their] purposes and policies." As of the date of publication, no such rules had been promulgated.

### **E. Purpose and Intent of Credit Provisions of Marital Property Act [§ 5.60]**

In addition to the general considerations involving construction of the Act, *see supra* § 5.19, the reasons for including the special provisions of the Act governing the obtaining and granting of credit should be recognized.

The movement to adopt community property in Wisconsin was largely based on four goals: (1) achievement of equal rights for spouses; (2) tax reform (i.e., tax-free interspousal transfers and joint income tax returns); (3) spousal equality in management and control during marriage and at death; and (4) equal access to credit by spouses. *See, e.g.,* Tony

Earl, *Tony Earl on Women's Issues* (Tony Earl for Governor Comm., no date); *see also* Anthony S. Earl, *Marital Property: Reform in the Wisconsin Tradition*, 68 Marq. L. Rev. 381 (1985).

In the marital property bills introduced in the 1979, 1981, and 1983 legislative sessions—whether in the form of “marital partnership property,” community property, alternatives to community property, or UMPA—special provisions were included in attempts to achieve equal access to credit. The Act’s provisions expanding the application of management and control rights and governing credit transactions with married persons are unique to Wisconsin and are additions to UMPA. Accordingly, these provisions are to be construed liberally and in a manner to achieve their purposes. *See* Wis. Stat. §§ 765.001(3), 766.001(1).

The following quote is from the March 8, 1984, major floor debate speech of State Senator Donald J. Hanaway, cosponsor of 1983 Senate Substitute Amendment 1 to Assembly Bill 200, which ultimately became the Act. It illustrates the importance and purpose of the Act’s unique credit provisions:

A non-uniform section [not included in UMPA] that has already been mentioned [is] the credit provisions. There is an argument as to whether or not the uniform law [UMPA] really does extend access to credit and get into the credit area. So that there was no question about our attitude about this problem in Wisconsin, we wanted to make it very clear in this bill that there was going to be access to credit for *all* spouses, and that’s why we included the credit provisions. It provides access, it requires creditors to consider the creditworthiness of both spouses, and the creditors, as indicated before, are fully protected.

*See also* Adelman et al., *supra* § 5.19, at 394.

## **V. Procedures in Creditor-Applicant Transactions [§ 5.61]**

### **A. In General [§ 5.62]**

Sections 5.63–.71, *infra*, set forth the procedures under section 766.56 that govern relationships between creditors and married persons, when a married person applies for credit based on marital property and the credit results in a family-purpose obligation.

## **B. Inquiry as to Marital Status and Marital Property Agreements [§ 5.63]**

A creditor may inquire as to the marital status of the applicant. Wis. Stat. § 766.56(2)(d). The ECOA also permits such an inquiry as long as it is intended to ascertain rights and remedies and not to discriminate in granting credit. 15 U.S.C. § 1691(b)(1). Further, in Wisconsin Consumer Act credit transactions, the creditor must give written notice to the nonapplicant spouse of the extension of credit. Wis. Stat. § 766.56(3)(b); *see infra* § 5.70. Accordingly, asking for the nonapplicant spouse's name and address would be necessary if information concerning marital status is not volunteered.

If the applicant is married, the creditor also may ask whether a marital property agreement exists, since such an inquiry is relevant to a determination of the extent of marital property available to satisfy the obligation and since there is no provision prohibiting such an inquiry. However, creditors are no longer *required* to inquire about the existence of a marital property agreement, as they were under the Act as originally adopted. *See* Wis. Stat. § 766.56(2)(b) (1983–84) (repealed and recreated by 1985 Trailer Bill). As noted in section 5.36, *supra*, the creditor is bound by the provisions of a marital property agreement if a copy is furnished by the applicant before the credit is granted. Wis. Stat. § 766.56(2)(c).

## **C. Effect of Marital Property Agreements, Unilateral Statements, and Court Decrees [§ 5.64]**

In Wisconsin Consumer Act transactions involving spouses, section 766.56(2)(b) requires the creditor to include a notice to the applicant in every written credit application. The notice must state that no provision of a marital property agreement, a unilateral statement electing to treat income on nonmarital property as individual property, or a court decree under the remedy provisions of the Act adversely affects the interest of the creditor unless the creditor, before granting the credit, is furnished a copy of the agreement, statement, or decree or has actual knowledge of the adverse provision when the obligation to the creditor is incurred. Wis. Stat. § 766.56(2)(b). Accordingly, in Consumer Act transactions, the applicant is alerted to the fact that provisions of such documents will not be binding on the creditor unless a copy of the relevant document is

given to the creditor (or the debtor can establish that the creditor had actual knowledge of the adverse provision) before the credit is granted. In credit transactions not governed by the Consumer Act, the creditor is not required to include a notice as to the effect of such agreements or decrees.

With respect to credit generally (i.e., not limited to Consumer Act transactions or credit transactions with a creditor who regularly extends credit), the Act provides that if the applicant discloses the existence of a marital property agreement or decree and provides a copy to the creditor before credit is granted (or, in the case of an open-end plan, before the plan is entered into), the creditor is bound by any property classification, characterization of an obligation, or management and control right contained in the document. Wis. Stat. § 766.56(2)(c); *see supra* §§ 5.45–.50 (definitions of credit and creditor).

If the disclosure of the marital property agreement, unilateral statement, or decree is made after the credit is granted (or after an open-end plan is entered into), the creditor is not bound by the provisions of the document with respect to that obligation (or plan), including any renewals, extensions, or modifications of the obligation or use of the plan. Wis. Stat. § 766.56(2)(c). Also, in credit transactions with spouses, the recording of a marital property agreement or a unilateral statement (or its revocation) with respect to income on nonmarital property does not constitute actual or constructive notice to third parties, except with respect to the application of chapter 706 regarding conveyancing. Wis. Stat. § 766.56(2)(a); *see supra* § 5.36.

➤ **Note.** With respect to the right of the nonapplicant spouse to terminate a Consumer Act open-end credit plan that may result in a family-purpose obligation, see sections 5.72–.75, *infra*. This right may be a significant remedy for the nonapplicant spouse if the applicant spouse fails to timely disclose to the creditor a marital property agreement, statement, or decree and the failure adversely affects the interests of the nonapplicant spouse.

➤ **Practice Tip.** The above provisions relating to the effects of undisclosed marital property agreements, unilateral statements, or court decrees are for the protection of the creditor. Accordingly, although there is no specific statutory provision, the creditor should be able to waive these provisions by agreeing to be bound by the

particular document after disclosure. The effect of such a waiver would be analogous to the binding effect of a written consent under section 766.55(4), signed by a creditor, that diminishes the creditor's rights provided in section 766.55 (obligations of spouses).

## **D. Predetermination Date Open-end Plans [§ 5.65]**

### **1. In General [§ 5.66]**

The Act contains a special section, section 766.555, relating to open-end plans that were established by one spouse before the spouses' determination date. Such plans are sometimes called *straddle accounts*. The purpose of section 766.555 is to clarify what property is available for satisfaction of family-purpose obligations incurred after the determination date by a spouse under such a plan. *See* Wis. Stat. Ann. § 766.555 Legis. Council Notes—1985 Act 37, § 99 (West 2009). Section 766.555(1)(a) defines an *open-end plan* as credit extended on an account pursuant to a plan that permits a spouse to make purchases or obtain loans directly from the creditor, or indirectly from the creditor by use of a credit card, check, or other device. Section 766.555 applies only to those plans for which only one of the spouses is a party to the account. Wis. Stat. § 766.555(1)(b).

Section 766.555 provides one set of provisions for spouses whose determination date is 12:01 a.m. on January 1, 1986, and another set for persons whose determination date is after 12:01 a.m. on January 1, 1986, discussed in sections 5.67 and 5.68, *infra*, respectively.

### **2. Spouses' Determination Date Is January 1, 1986 [§ 5.67]**

With respect to pre-Act open-end plans (i.e., when the spouses' determination date is January 1, 1986), an obligation incurred on or after January 1, 1986, under the plan by the spouse who entered into the plan—whether or not the obligation is a family-purpose obligation—may be satisfied only from

1. Nonmarital property of that spouse; and

2. That part of marital property that would have been the property of that spouse except for the enactment of the Marital Property Act.

Wis. Stat. § 766.555(2)(b). That is, obligations under pre-Act plans are treated in the same way as pre-Act obligations. *See* Wis. Stat. § 766.55(2)(c)2. However, before the date that such a family-purpose obligation is incurred, the creditor may give written notice to both spouses describing the nature of the plan and stating that a family-purpose obligation incurred under the plan may be satisfied from *all* marital property of the spouses, including the income of both, and from the property of the incurring spouse that is not marital property. *See* Wis. Stat. § 766.555(2)(c)1., 2. Then, the obligation may be satisfied from all marital property of the spouses, in addition to the above-described property of the spouse who entered into the plan. *Id.*

The written notice described above is considered given on the date that the creditor mails it. Wis. Stat. § 766.555(2)(c)3. It may be enclosed in an envelope addressed to the incurring spouse at his or her last-known address, if a statement appears on the face of the envelope that alerts both spouses that the envelope contains important information for both of them. Wis. Stat. § 766.555(2)(c)4.

### **3. Spouses' Determination Date Is After January 1, 1986 [§ 5.68]**

As noted in section 5.67, *supra*, pre-Act open-end plans are subject to a special notice provision enabling a creditor who complies with the provision to reach all marital property of the spouses, in addition to the incurring spouse's nonmarital property and that part of marital property that would have been the incurring spouse's property but for the enactment of the Act. *See* Wis. Stat. § 766.555(2)(c)1., 2. There is no corresponding notice provision for predetermination date open-end plans of persons who marry after January 1, 1986, or of spouses who become domiciled in Wisconsin after January 1, 1986 (i.e., when the spouses' determination date is *after* January 1, 1986). A notice requirement was not included because "there is no practical way for a creditor to routinely give such a notice under the circumstances addressed by [these statutory provisions]." Wis. Stat. Ann. § 766.555 Legis. Council Notes—1985 Act 37, § 99 (West 2009). However, notwithstanding the lack of a notice provision, a family-purpose obligation incurred after the determination date under such a predetermination date open-end plan may be satisfied

from all marital property and all other property of the incurring spouse. Wis. Stat. § 766.555(3)(c). This is consistent with the general rule governing family-purpose obligations. *See* Wis. Stat. § 766.55(2)(b). On the other hand, a *nonfamily-purpose* obligation incurred after the determination date under such a predetermination date open-end plan may be satisfied only from nonmarital property of that spouse and from that part of marital property that would have been the property of that spouse but for the enactment of the Act. *See* Wis. Stat. § 766.555(3)(b). This is consistent with the general rule governing pre-Act obligations incurred by a spouse. *See* Wis. Stat. § 766.55(2)(c)2.

#### **4. Conclusion [§ 5.69]**

The difference between predetermination date open-end plans for spouses whose determination date is January 1, 1986, and predetermination date plans for spouses whose determination date is after January 1, 1986, is that in the former case, family-purpose obligations cannot be satisfied from all marital property unless the notice described in section 766.555(2)(c)2. is given to both spouses. *See* Wis. Stat. § 766.555(2)(c)1.

#### **E. Notice to Nonapplicant Spouse of Extension of Credit to Applicant Spouse [§ 5.70]**

When a creditor extends credit to a spouse in a Consumer Act transaction and the extension of credit may result in a family-purpose obligation, section 766.56(3)(b) requires the creditor to give notice to the nonapplicant spouse (sometimes referred to as the tattletale notice) before any payment is due. This notice requirement applies to an extension of credit under a postdetermination date open-end credit plan, as defined in the Wisconsin Consumer Act, *see* Wis. Stat. § 421.301(27); it also applies to Consumer Act credit other than open-end credit extended after the determination date. Wis. Stat. § 766.56(3)(a). But the notice requirement does not extend to renewals, extensions, modifications, or the use of an open-end plan. *Id.* Predetermination date open-end credit plans are governed by section 766.555. *See supra* §§ 5.65–.69.

A creditor may satisfy the notice requirement by providing a copy of the document evidencing the obligation or any required credit disclosure



that is given to the applicant spouse or by providing a separate written description of the nature of the credit extended. Wis. Stat. § 766.56(3)(b). The notice is considered given on the date it is mailed to the address of the nonapplicant spouse provided by the applicant spouse. If the applicant informs the creditor that the spouses reside at the same address, the notice may be enclosed in an envelope addressed to the nonapplicant spouse or both spouses. *Id.* Notice is also deemed given if the nonapplicant spouse has actual knowledge of the credit extension or waives the notice requirement in writing. Wis. Stat. § 766.56(3)(c).

➤ **Comment.** The notice requirement under section 766.56(3)(b) refers to an extension of credit that “may result in” a family-purpose obligation. Thus, the requirement covers a line of credit, such as the creation of a charge account or issuance of a credit card, that may or may not be used for a family-purpose obligation. It is arguable that, for example, on issuance of a credit card that may be used for a family purpose, the creditor may reach all marital property assets under section 766.55(2)(b) even if a particular charge—or, indeed, all charges—made on the card were not incurred in the interest of the marriage or the family. *See infra* ch. 6; *see also supra* § 5.42, *infra* § 5.71 (effect of separate written statement relating to family purpose under section 766.55(1)).

The Marital Property Act added section 427.104(2) to the Consumer Act to provide that if notice is given under section 766.56(3)(b), sending a billing statement or other notice of account to the spouse of the debtor or collecting the amount due on the account from the spouse of the debtor does not in itself constitute a prohibited practice under section 427.104. *See infra* § 6.69 (general relationship between Marital Property Act and Wisconsin Consumer Act); *see also infra* §§ 5.72–.75.

Other than the \$25 liability provided under section 766.56(4)(b) for failure to give the notice to the nonapplicant, *see supra* § 5.57, section 766.56 does not specifically state any consequences of providing or failing to provide the notice. In *Park Bank-West v. Mueller*, 151 Wis. 2d 476, 444 N.W.2d 754 (Ct. App. 1989), the court held that a creditor’s rights were not affected by the creditor’s failure to give the “tattletale notice” to the nonincurring spouse under section 766.56(3)(b). In pointing out that the only penalty was a \$25 liability provided in section 766.56(4)(b), the court concluded that the notice was informational only and that the legislature had not intended that a creditor’s right to reach marital property assets be limited by its failure to give notice. *Id.* at 484.

The court criticized this result because of its adverse effect on the spouse who does not receive the notice and suggested that the legislature reevaluate the effect of section 766.56(4)(b). *Id.* at 484–85.

➤ **Practice Tip.** As a practical matter, particularly when significant Consumer Act credit is involved and marital property is relied on because the applicant spouse's nonmarital property is insufficient to support the credit, it may be in the creditor's interest to mail full information under section 766.56(3)(b) to the nonapplicant spouse, including copies of the application, all other credit documents, a listing of all property relied on, and the asserted classification of that property. However, a creditor who gives the above notice probably will not estop the nonapplicant spouse from contending that the property asserted by the applicant spouse to be marital property was in fact the nonapplicant's individual or predetermination date property.

## **F. Conclusiveness of Family-purpose Statement**

### **[§ 5.71]**

Under section 766.55(1), if an obligated or incurring spouse signs a statement at or before the time an obligation is incurred, stating that the obligation is or will be incurred in the interest of the marriage or the family, the obligation will be considered a family-purpose obligation. The statement is “conclusive evidence that the obligation to which the statement refers is an obligation in the interest of the marriage or family” with respect to the rights of the creditor, regardless of the actual use of the credit. Wis. Stat. § 766.55(1). The statement does not, however, affect any interspousal right or remedy. *Id.*

It should be noted that the family-purpose statement under section 766.55(1) applies to any “obligation.” It is not limited to Consumer Act credit or credit transactions with a creditor who regularly extends credit. Such a separate statement signed by the spouse who is obtaining credit or incurring an obligation will be sufficient to protect the creditor or obligee from any later assertion by either spouse that the obligation was not for a family purpose. Accordingly, the creditor is assured of being able to reach all marital property to satisfy the obligation, provided the statement is signed at or before the time the obligation is incurred.

➤ **Historical Note.** The Marital Property Act as originally adopted lacked any provision for a family-purpose statement. Thus, a creditor relying on marital property in extending credit took the risk that the obligation being incurred would not be found to be a family-purpose obligation. Either or both spouses appeared to be free to contest a creditor's assertion that the obligation was incurred for a family purpose and hence might contend that the creditor could not reach all marital property. To remedy this, the 1985 Trailer Bill amended section 766.55(1) to provide for the family-purpose statement.

## **VI. Relationship of Marital Property Act to Consumer Act and Other Laws [§ 5.72]**

### **A. Consumer Act [§ 5.73]**

Section 766.565 attempts to harmonize a number of the provisions of the Consumer Act with the Marital Property Act. These harmonizing provisions include the following:

1. Section 766.565(3) provides that the spouse of a person who incurs a family-purpose obligation that is governed by the Consumer Act may exercise the rights and remedies that are available to the incurring spouse under the Consumer Act.
2. Section 766.565(5) provides that the spouse of a person who establishes an open-end credit plan governed by the Consumer Act that may result in a family-purpose obligation may terminate the plan (with consequences provided in the statute) by giving written notice of termination to the creditor. *See infra* § 5.74 (relationship between unilateral termination provision of section 766.565(5) and ECOA and Regulation B). An open-end plan may include a provision authorizing the creditor to declare the account balance due and payable on receipt of notice of termination. Wis. Stat. § 766.565(5).
3. Section 766.565(6) provides that written notice to a spouse under the Consumer Act concerning an increase in the finance-charge rate is not effective with respect to the interest of the nonincurring spouse in marital property unless notice of the increase is given to both spouses.

## B. Equal Credit Opportunity Act [§ 5.74]

In 1986, the Federal Reserve Board (FRB) issued a notice of intent to make a preemption determination regarding certain provisions of the Marital Property Act, including section 766.565(5), discussed in section 5.73, *supra*. See Equal Credit Opportunity; Intent to Preempt Wisconsin Law, 51 Fed. Reg. 35,521 (1986). In the notice, the FRB published for comment a proposed determination that the unilateral-termination provision of section 766.565(5) is inconsistent with, and therefore preempted by, the ECOA and Regulation B. The FRB viewed the practical effect of section 766.565(5) as nullifying a married applicant's right to obtain individual credit, contrary to section 202.7(a) of Regulation B, which prohibits creditors from refusing to grant an individual account to a creditworthy applicant on the basis of marital status. See 12 C.F.R. § 202.7(a).

In its decision, effective November 1, 1987, the FRB ultimately determined not to preempt the specified provisions of the Wisconsin Marital Property Act. 52 Fed. Reg. 35,537 (1987), *reprinted* in 73 Fed. Reserve Bull. 869 (Nov. 1987). The FRB further concluded that Wisconsin is a community property state for Regulation B purposes and that specified sections of the Wisconsin Statutes are not preempted by Regulation B.

The FRB stated that although a clear inconsistency exists between section 766.565(5) and the Regulation B provision prohibiting discrimination based on marital status, *see* 12 C.F.R. § 202.7(a), section 766.565(5) is entitled to deference under the ECOA provision stating that consideration or application of state laws directly or indirectly affecting creditworthiness does not constitute discrimination, 15 U.S.C. § 1691d(b). The FRB thus decided not to preempt section 766.565(5), based on the ECOA and Regulation B provisions allowing a creditor to take into account state property law affecting creditworthiness. See 15 U.S.C. § 1691d(b); 12 C.F.R. § 202.6(c).

The FRB also examined section 766.56(2)(d) and concluded that the statutory language allowing a creditor to ask whether a credit applicant is "married, unmarried or separated, [or] under a decree of legal separation" is not mandatory and only clarifies the nature of the inquiry permissible by a creditor when a person applies for credit. The FRB decided that inquiries involving the applicant's marital status under subsections 766.56(2)(d) and (3)(b), as well as the required name and address of the

applicant's spouse under section 766.56(3)(b), do not conflict with the ECOA or Regulation B. *See also supra* §§ 5.63 (inquiry as to marital status), 5.70 (notice to nonapplicant spouse), *infra* §§ 5.80, .91–.96 (applicability of ECOA and conclusion that Wisconsin is community property state for purposes of ECOA).

### **C. Truth in Lending Act [§ 5.75]**

Questions have been raised about whether the application of section 766.565(5), discussed in section 5.73, *supra*, violates the Truth in Lending Act (TILA), 15 U.S.C. §§ 1601–1667f, or Regulation Z (Truth in Lending), 12 C.F.R. pt. 226. Specifically, the question arises whether an open-end plan that includes a provision under section 766.565(5) permitting the creditor to declare the balance due on receipt of notice of termination by the nonincurring spouse violates either the TILA or Regulation Z.

Under Regulation Z, a creditor must make certain written disclosures to the consumer regarding the terms and conditions of open-end credit and home-equity plans. *See* 12 C.F.R. § 226.5. For example, for home-equity plans, the statement to the consumer must include the conditions under which the creditor may terminate credit and demand full payment. 12 C.F.R. § 226.5b(d)(4). No such creditor under a home-equity plan, by contract or otherwise, may so terminate and demand full payment except for the consumer's fraud or misrepresentation, failure to meet repayment terms, or action or inaction that has adversely affected the creditor's security or the creditor's rights in the security. 12 C.F.R. § 226.5b(f)(2)(i)–(iii). These regulations were adopted by the FRB effective June 7, 1989, and compliance became mandatory as of November 7, 1989. Truth in Lending; Home Equity Disclosure and Substantive Rules, 54 Fed. Reg. 24,670 (1989). Federal law dealing with credit extended by a depository institution to its executive officers specifically requires that as a condition of the plan the credit becomes due and payable on demand, provided that the creditor includes such a provision in the initial agreement. 12 C.F.R. § 226.5b(f)(2)(iv).

Note that the exceptions listed above, which permit the creditor under a home-equity plan to accelerate payment, do not include third-party actions such as the consumer's spouse's termination of the plan under section 766.565(5). The question arises whether a creditor under a home-equity plan (and possibly in other situations governed by

Regulation Z) may include a provision authorizing the creditor to accelerate the balance of an open-end plan after receiving notice of termination by the nonincurring spouse. The FRB considered this issue and published notice of its intent to make a preemptive determination that such a provision in a home-equity plan conflicts with the TILA and the applicable provisions of Regulation Z, *see* 12 C.F.R. § 226.5b(f)(2). Truth in Lending; Intent to Make Determination of Effect on State Law; Wisconsin, 55 Fed. Reg. 13,282 (1990).

In another decision, effective October 1, 1991, the FRB determined that the portion of section 766.565(5) that permits a creditor to include in an open-end home equity plan agreement a provision authorizing the creditor to accelerate the balance due after receiving notice of termination from the nonobligated spouse is inconsistent with the purposes of federal law, *see* 12 C.F.R. § 226.5b(f)(2), and therefore is preempted by federal law. Truth in Lending; Determination of Effect on State Law (Wisconsin), 55 Fed. Reg. 31,815 (1990). But in the same decision, the FRB ruled that valid reasons exist for *not* preempting the portion of section 766.565(5) that permits the nonobligated spouse to terminate the plan. These include an interest in protecting the nonobligated spouse's marital property rights (by deeming the spouse a "consumer" for purposes of terminating the plan) and the precedent for considering a nonobligated person (who has an ownership interest in an asset that secures the plan) a "consumer" who can terminate the plan. The FRB found no similar basis for permitting a creditor to accelerate the balance, since that would "interfere with the operation of the federal scheme" that restricts creditors' actions. *Id.* at 31,816. These federal provisions were designed to protect the borrower from such an adverse result except in limited circumstances provided in Regulation Z. *See* 12 C.F.R. § 226.5b(f)(2).

The above preemptive determination is now reflected in the official staff commentary on Regulation Z. *See* 12 C.F.R. pt. 226, Supp. I cmt. 28(a)-15. One result of the determination may be illustrated by the following example.

➤ **Example.** Assume that a husband established a line of credit under an open-end plan covered by the TILA, secured by the spouses' dwelling, but that the husband was the only spouse obligated under the plan. Assume also that the plan permitted the creditor to accelerate the balance due after receiving notice from the nonobligated spouse terminating the plan under section 766.565(5).

If the wife gives such notice, it would appear that the plan has been terminated as to the husband's right to obtain future advances under the plan, but that the creditor may not accelerate payment of the debt then outstanding under the plan. It would appear that the outstanding balance would continue to be payable in installments as if the plan had not been terminated.

➤ **Note.** As issued, the above determination applies only to open-end plans secured by a consumer's dwelling, covered by the TILA. Previously, the FRB had determined that no part of section 766.565(5) was preempted by the ECOA and Regulation B. Equal Credit Opportunity; Determination of Effect of State Laws (Wisconsin). 52 Fed. Reg. 35,537 (1987); *see supra* § 5.74. However, as discussed above, the portion of section 766.565(5) permitting acceleration under a home-equity plan after receipt of a termination notice covered by the TILA has been determined to be preempted by that Act and Regulation Z.

Regulation Z applies if credit is primarily for family, personal, or household purposes. 12 C.F.R. § 226.1(c)(1)(iv). Credit for a business, commercial, agricultural, or organizational purpose is exempt. 12 C.F.R. § 226.3(a)(1). However, obligations incurred for a "business purpose" and those incurred "in the interest of the marriage or the family" are not necessarily mutually exclusive. A spouse who guarantees an obligation of a corporation in which he or she works has a business purpose in signing the guarantee; yet the obligation under the guarantee is in the interest of the guarantor's marriage or family. The guarantee may enable the corporation to obtain a loan that will enable its business to continue, thereby supporting the guarantor and his or her family. A business-purpose credit includes a loan to expand a business, even if it is secured by the borrower's residence or personal property. 12 C.F.R. pt. 226, Supp. I cmt. 3(a)-2.

As noted in section 5.71, *supra*, a family-purpose statement under section 766.55(1) is considered "conclusive evidence" that the obligation in question is an obligation in the interest of the marriage or family. However, a family-purpose statement is intended only to expand the property available to creditors, not to eliminate the business-purpose exception of Regulation Z. The primary purpose of an underlying loan must be examined to determine whether a transaction is subject to Regulation Z and the federal Truth in Lending Act. In *Poe v. First National Bank*, 597 F.2d 895 (5th Cir. 1979), for example, a

corporation's principal shareholder and his wife signed guarantees and pledged the family home as security for various notes evidencing loans to the corporation. The court stated that

The Truth-in-Lending Act specifically exempts from its scope extensions of credit for business or commercial purposes. As to consumer credit transactions, the Act provides that the adjective "consumer" is specifically intended to characterize the transaction as one in which the party to whom credit is extended is a natural person and the money is primarily for personal, family, household, or agricultural purposes . . . . The courts will look to the purpose of the loan to determine whether it is covered by the Act. In the instant case, there is no question that the purpose of each transaction was to finance the corporation. The transactions, therefore, were exempted from the Act.

*Id.* at 896 (citations omitted); *see also Toy Nat'l Bank v. McGarr*, 286 N.W.2d 376, 378 (Iowa 1979) (holding that "not every loan transaction which results in a security interest in the debtor's residence is subject to this statutory right of rescission [found in the TILA]. The transaction must be otherwise subject to the Act, i.e., it must be a consumer loan rather than a business or commercial one.").

## **VII. Effect of Equal Credit Opportunity Act on Credit Transactions Under Wisconsin Marital Property Act**

### **[§ 5.76]**

#### **A. ECOA in General [§ 5.77]**

In the early 1970s, the National Commission on Consumer Finance reported evidence of widespread discrimination against women in the credit industry. For example, women were at times required to answer questions on credit application forms that addressed age, sex, race, religion, birth-control practices, and childbearing intentions. Susan Smith Blakely, *Credit Opportunity for Women: The ECOA and Its Effects*, 1981 Wis. L. Rev. 655, 656. Seeking to protect married women from discriminatory credit practices that prohibited them from establishing individual credit, Congress passed the ECOA in 1974 and expanded it in 1976. Equal Credit Opportunity Act, Pub. L. No. 93-495, 88 Stat. 1521 (1974) (codified at 15 U.S.C. §§ 1691–1691f), *amended by* Equal Credit Opportunity Act Amendments of 1976, Pub. L. No. 94-239, 90 Stat. 251. The ECOA is Title VII of the Consumer Credit Protection



Act. The Consumer Credit Protection Act originally consisted of five titles and was adopted in 1968 (and mainly imposed standard disclosure requirements on transactions covered by that act). *See* Consumer Credit Protection Act, Pub. L. No. 90-321, 82 Stat. 146 (1968) (codified at 15 U.S.C. §§ 1601–1693r). The Fair Credit Reporting Act (FCRA) was added as Title VI of the Consumer Credit Protection Act in 1970. *See* Fair Credit Reporting Act, Pub. L. No. 91-508, 84 Stat. 1128 (1970) (codified at 15 U.S.C. §§ 1681–1681u); *see also infra* § 5.82.

The ECOA prohibits discrimination at all stages of a credit transaction, including any extensions of credit to individuals, small businesses, partnerships, trusts, or corporations; credit investigations, creditworthiness standards, signature requirements, and credit reporting; and collection of debts. The prohibitions against discrimination are not limited to banks and financial institutions under the ECOA. The ECOA differs from other areas of the Consumer Credit Protection Act in that it applies to business and commercial transactions and to any individual who regularly extends credit. *See infra* § 5.79 (definitions of creditor and person under ECOA).

The burden of proof in an ECOA case is similar to that in any other type of discrimination case. *See Cragin v. First Fed. Savs. & Loan Ass’n*, 498 F. Supp. 379, 384 (D. Nev. 1980). If a claimant makes out a prima facie case by showing that the party is a member of a class protected by the law preventing discrimination, the burden shifts to the creditor to establish a nondiscriminatory basis for its actions. *See McDonnell Douglas Corp. v. Green*, 411 U.S. 792, 802–03 (1973).

## **B. General Applicability of ECOA [§ 5.78]**

### **1. Introduction [§ 5.79]**

In a community property state, as in a common-law property state, a number of questions about the granting of credit by commercial lenders to married persons are governed by the ECOA. (Wisconsin is a community property state for purposes of the ECOA. *See infra* §§ 5.87–.90.) The ECOA, which became effective on October 28, 1975, applies to creditors who regularly extend, renew, or continue consumer credit. The ECOA defines the term *creditor* as “any person who regularly extends, renews, or continues credit; any person who regularly arranges for the extension, renewal, or continuation of credit; or any assignee of

an original creditor who participates in the decision to extend, renew, or continue credit.” 15 U.S.C. § 1691a(e). The term *person* as used in the ECOA is also broadly defined. See 15 U.S.C. § 1691a(f) (defining person as “a natural person, a corporation, government or governmental subdivision or agency, trust, estate, partnership, cooperative, or association”).

The purpose of the ECOA is “to require that financial institutions and other firms engaged in the extension of credit make that credit equally available to all creditworthy customers without regard to sex or marital status.” Pub. L. No. 93-495, tit. V, § 502, 88 Stat. 1521 (1974) (codified at 15 U.S.C. § 1691 note). This purpose is carried out by prohibiting discrimination by any creditor with regard to any aspect of a credit transaction on the basis of prohibited factors, including sex and marital status. The ECOA provides as follows:

- (a) It shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction—
  - (1) on the basis of ... sex or marital status ... ;
- (b) It shall not constitute discrimination for purposes of this subchapter for a creditor—
  - (2) to make an inquiry of marital status if such inquiry is for the purpose of ascertaining the creditor’s rights and remedies applicable to the particular extension of credit and not to discriminate in a determination of credit-worthiness....

15 U.S.C. § 1691(a), (b). To *discriminate* against a credit applicant is defined in Regulation B as meaning “to treat an applicant less favorably than other applicants.” 12 C.F.R. § 202.2(n). This means to treat an applicant less favorably than others similarly situated, on the basis of an impermissible factor.

The FRB is broadly directed to prescribe regulations “to carry out the purposes” of the ECOA. 15 U.S.C. § 1691b(a)(1). The FRB is also authorized to exempt transactions that are not “primarily for personal, family, or household purposes.” 15 U.S.C. § 1691b(a)(2). However, administrative enforcement of the ECOA with respect to various categories of creditors is diffused among various agencies, such as the Comptroller of the Currency, the FRB, and the Securities and Exchange Commission. See 15 U.S.C. § 1691c(a). When the ECOA does not specifically commit enforcement to a particular federal agency (as is the case with consumer-finance companies), the Federal Trade Commission (FTC) is charged with enforcing the ECOA’s requirements; the FTC is

empowered to enforce any board regulation under the ECOA as if the violation had been a violation of an FTC trade-regulation rule. 15 U.S.C. § 1691c(c).

Penalties imposed on creditors who violate the ECOA include recovery in federal court of actual damages (including recovery by class action) and punitive damages (including class-action punitive damages). Costs of the action and reasonable attorney fees are to be added to damages awarded. 15 U.S.C. § 1691e(d); *see also Anderson v. United Fin. Co.*, 666 F.2d 1274 (9th Cir. 1982) (discussing actual and punitive damages and attorney fees recoverable under ECOA).

There is a two-year statute of limitation on actions for relief under the ECOA seeking damages, attorney fees, and costs. 15 U.S.C. § 1691e(f). No such statute of limitation exists for defensive assertions of the ECOA to block a lender's attempt to enforce a credit instrument. *See, e.g., Silverman v. Eastrich Multiple Inv. Fund, L.P.*, 51 F.3d 28, 32 (3d Cir. 1995) (holding that "[c]laims by way of recoupment are 'never barred by the statute of limitations ... '" (quoting *Bull v. United States*, 295 U.S. 247, 262 (1935))).

Section 425.307(1) sets forth the statute of limitation for actions brought under the Wisconsin Consumer Act. A customer must generally bring an action to enforce rights under chapters 421–427 within (1) one year after the date of the last violation, (2) two years after the consummation of the agreement, or (3) one year after the last payment is made, whichever is later. Wis. Stat. § 425.307(1). Actions with respect to transactions under open-end credit plans must be commenced within two years after the date of the last violation. No action under the Wisconsin Consumer Act may be commenced more than six years after the date of the last violation. *Id.*

## **2. General Relationship Between State Law and ECOA [§ 5.80]**

To ensure the availability of community property or income to satisfy credit obligations, many creditors in community property states have taken the position that before granting the applicant spouse's request for credit, the credit grantor is justified in requesting the signature of the nonapplicant spouse on the credit application and the credit instruments involved. *See Loeb, supra* § 5.42; *Brown, supra* § 5.42. The effect of

the nonapplicant spouse's signature, of course, is to create personal liability on the part of that spouse; hence, the creditor can also reach that spouse's noncommunity property assets (i.e., separate property of that spouse).

➤ **Note.** When considering ECOA enforcement and cases from other states, one should be aware that the laws of the other community property states vary and may not include the broad provisions contained in the Wisconsin Marital Property Act regarding management and control, property classification, family-purpose obligations, and assets available to satisfy obligations.

Provisions of the ECOA itself bear directly on the effect of state law on the ECOA. First, a request for signatures of both spouses for the purpose of creating a valid lien, passing clear title, or assigning earnings does not constitute discrimination under the ECOA as long as sex or marital status is not taken into account in evaluating creditworthiness. 15 U.S.C. § 1691d(a). Second, considering or applying state property laws affecting creditworthiness does not constitute discrimination under the ECOA. 15 U.S.C. § 1691d(b).

### **3. Information Requested on Credit Applications** **[§ 5.81]**

Under Regulation B, a creditor may request information concerning an applicant's spouse if (1) the spouse will be permitted to use the account, (2) the spouse will be contractually liable on the account, (3) the applicant is relying on the spouse's income as a basis for repayment of the requested credit, (4) the applicant resides in a community property state, or (5) property relied on as a basis for repayment is located in a community property state. 12 C.F.R. § 202.5(c)(2). If an applicant applies for an individual unsecured account and resides in a community property state (or if property relied on as a basis for repayment is located in such a state), a creditor may request information concerning the applicant's marital status. 12 C.F.R. § 202.5(d)(1).

#### 4. Credit Reports Concerning Nonapplicant Spouse [§ 5.82]

Implicit in Regulation B is an assumption that, in a community property state, in addition to requesting information from the applicant spouse concerning the nonapplicant spouse, the creditor may consider the nonapplicant spouse's credit history and obtain credit information from other sources. This follows, since the creditor has a legitimate business need for the information, and thus meets the requirements of the FCRA. *See* 15 U.S.C. § 1681b(a)(3)(F) ("any consumer reporting agency may furnish a consumer report ... [t]o a person which it has reason to believe ... has a legitimate business need for the information ... in connection with a business transaction that is initiated by the consumer").

In general, the FCRA regulates organizations that are in the business of supplying credit information. The general purposes of the FCRA are to protect the credit reputation of a consumer and to prevent the dissemination of inaccurate credit information concerning consumers. The FTC has issued unofficial staff interpretations of the provisions of the FCRA, consistent with its responsibility when applying both the ECOA and the FCRA to review and regulate commercial activity it concludes is unfair or deceptive.

An FTC unofficial staff interpretation dated May 29, 1976, concerning the FCRA took the position that a credit grantor has a "legitimate need" for the credit report of a nonapplicant spouse when the applicant relies on community property to qualify for credit. *See* L. Goldfarb, Div. of Special Statutes, FTC Unofficial Staff Interpretation (Mar. 29, 1976). The rationale of the opinion is that the credit extension "involves" the nonapplicant spouse because the extension entails pledging (or relying on) the resources of both spouses (i.e., the community property). *Id.*

There is a question whether a spouse in a community property state where each spouse has an equal right to manage and control community assets has a right to obtain a credit report concerning his or her spouse. Under the FCRA, the spouse arguably has a legitimate business need for the information, to the extent that the information requested concerns assets that constitute community property. *See Fernandez v. Retail Credit Co.*, 349 F. Supp. 652, 654–55 (E.D. La. 1972) (interpreting 15 U.S.C. § 1681b(3)(F) and holding that "legitimate business need[s] ... in

connection with a business transaction” related to needs and objectives of person to whom report is furnished, rather than to business needs of subject of report). This interpretation, if correct, places a practical burden on the credit agency to determine what assets constitute community property, because there would be no “legitimate need” to know information concerning the nonapplicant spouse’s separate property. However, in Wisconsin, this burden should be eased by the presumption that all assets of spouses are marital property. *See Wis. Stat. § 766.31(2)*. Further, in Wisconsin, it appears that credit information concerning the other spouse “involves” the applicant spouse, since credit actions of the other spouse affect the spouses’ marital property on which the applicant spouse may be relying.

In addition to the above considerations, Regulation B states that it does not limit or abridge any federal or state law regarding privacy or privileged information. *See* 12 C.F.R. § 202.5 n.1.

The issuance of an erroneous credit report regarding one spouse may form the basis of a claim by the other spouse under the FCRA if the other spouse’s ability to obtain credit is adversely affected. *See Williams v. Equifax Credit Info. Servs.*, 892 F. Supp. 951 (E.D. Mich. 1995) (holding that wife had standing to sue under FCRA because erroneous credit information about husband impaired wife’s own ability to secure credit on jointly owned property).

## **5. Evaluation of Applicant’s Credit [§ 5.83]**

Under Regulation B’s general rule on evaluating creditworthiness, a creditor may consider any information that the creditor obtains, except as otherwise provided in the ECOA or Regulation B, as long as the information is not used to discriminate against the applicant on a prohibited basis. 12 C.F.R. § 202.6(a). Regulation B states that, except as provided in the ECOA and Regulation B, a creditor “shall not take a prohibited basis into account in any system of evaluating the creditworthiness of applicants.” 12 C.F.R. § 202.6(b)(1). A creditor may, however, consider an applicant’s marital status “for the purpose of ascertaining the creditor’s rights and remedies applicable to the particular extension of credit.” 12 C.F.R. pt. 202, Supp. I cmt. 6(b)(8)-1. In addition, a creditor must not discount or exclude from consideration income of the applicant or the applicant’s spouse because of a prohibited basis; a creditor may consider “the amount and probable continuance of

any income in evaluating an applicant's creditworthiness." 12 C.F.R. § 202.6(b)(5). Finally, a creditor's consideration or application of state property laws affecting creditworthiness does not constitute unlawful discrimination for the purposes of the ECOA or Regulation B. 12 C.F.R. § 202.6(c); 15 U.S.C. § 1691d(b).

In evaluating credit, to the extent that a creditor considers credit history, the creditor is specifically authorized by Regulation B to consider the credit history of accounts that either spouse is permitted to use or for which both are liable. 12 C.F.R. § 202.6(b)(6)(i). In addition, to the extent that the creditor considers credit history, on the applicant's request the creditor must consider the credit history of any account in the name of the nonapplicant spouse "that the applicant can demonstrate accurately reflects the applicant's creditworthiness." 12 C.F.R. § 202.6(b)(6)(iii).

## **6. Spousal Signature Requirements [§ 5.84]**

### **a. Unsecured Credit [§ 5.85]**

Except as otherwise provided in section 202.7(d) of Regulation B, a creditor may not require the signature of an applicant's spouse (unless it is a joint application) on any credit instrument if the applicant qualifies under the creditor's standards of creditworthiness for the credit requested. 12 C.F.R. § 202.7(d)(1). This regulation was judicially recognized and enforced in *Anderson v. United Finance Co.*, 666 F.2d 1274 (9th Cir. 1982) (common-law-state transaction). Although the applicant in *Anderson* who requested credit in her sole name was found creditworthy by the creditor, the creditor required the applicant's spouse to sign the promissory note (in addition to the necessary security instrument to perfect a valid lien against property offered as security). In holding for the applicant, the court stated that this was not simply a technical violation, but rather it was "just the type of discrimination which the [Equal Credit Protection] Act was created to prohibit." *Id.* at 1276.

If the credit is unsecured and the applicant relies in part on property to establish creditworthiness, the creditor may consider state law; the form of ownership of the property; the property's susceptibility to attachment, execution, severance, or partition; and other factors that may affect the value to the creditor of the applicant's interest in the property. *See* 12

C.F.R. pt. 202, Supp. I cmt. 7(d)(2)-1, -2. However, if an applicant for unsecured credit resides in a community property state, the creditor may require the nonapplicant spouse's signature on an instrument necessary to make the community property available to satisfy the debt only if state law *denies* the applicant spouse power to manage or control sufficient community property to qualify for the credit requested and if the applicant's separate property is insufficient. 12 C.F.R. § 202.7(d)(3); *see also infra* §§ 5.87–.90.

With respect to a cosigner of credit applications and credit instruments, Regulation B is specific. A cosigner or guarantor may be requested only “[i]f, under a creditor’s standards of creditworthiness, the personal liability of an additional party is necessary to support the extension of the credit requested.” 12 C.F.R. § 202.7(d)(5). A creditor is not permitted to require that the spouse be the additional party. *Id.* However, if an applicant in a community property state relies on the spouse's future earnings that, as a matter of state law, cannot be characterized as community property until earned, the creditor may require the spouse's signature. 12 C.F.R. pt. 202, Supp. I cmt. 7(d)(5)-2.

## **b. Secured Credit [§ 5.86]**

As discussed in section 5.85, *supra*, the basic rule of Regulation B is that a creditor may not require the signature of the applicant's spouse (or the signature of another person) on a credit instrument, unless it is a joint application, “if the applicant qualifies under the creditor’s standards of creditworthiness for the amount and terms of the credit requested.” 12 C.F.R. § 202.7(d)(1). This rule applies to secured as well as unsecured credit. In the case of secured credit, however, a creditor may require the signature of the applicant's spouse on any instrument necessary or reasonably believed to be necessary under state law “to make the property being offered as security available to satisfy the debt in the event of default.” 12 C.F.R. § 202.7(d)(4). This includes any instrument needed to create a lien, pass clear title, or assign earnings. *Id.*; *see also McKenzie v. U.S. Home Corp.*, 704 F.2d 778 (5th Cir. 1983) (holding that creditor's requirement, involving Texas law, that applicant's husband execute deed of trust to ensure valid lien was not impermissible discrimination).

In granting secured credit under the Wisconsin Marital Property Act, a credit grantor is not prohibited by Regulation B from requiring the



other spouse to join in a security instrument if the applicant needs to use marital property held by the nonapplicant spouse as security to establish creditworthiness, or if the applicant does not have sole management and control rights over the property and lacks the power to encumber the assets. *See* Wis. Stat. § 766.51(1m); *see also supra* §§ 5.12–.26, *infra* § 5.126.

As a practical matter, to obtain priority with respect to third parties (such as bona fide purchasers and creditors), a lien against property must be perfected and notice provided. Accordingly, the ECOA provides that if perfection is required to meet a creditor's standards for creditworthiness, the nonapplicant spouse's signature may be required on the document creating the lien or secured interest if the signature is necessary to perfect the lien or create the secured interest and to provide effective notice to third parties. (This provision assumes, of course, that the creditor's requirements do not discriminate on an impermissible basis.) However, the creditor may not require the nonapplicant spouse's signature on any document obligating that spouse (for example, as a co-signer or guarantor), since the signature rules remain applicable to both secured and unsecured credit.

With respect to the effect of the Wisconsin Marital Property Act on secured credit documentation, as well as the provisions of the Uniform Commercial Code, *see* sections 5.129–.135, *infra*.

Lenders should be careful in requiring a spouse to sign a *note* when the other spouse qualifies independently as creditworthy. In granting secured credit under the Marital Property Act, a credit grantor is not prohibited by Regulation B from requiring both spouses to join in a *security instrument* if the applicant does not have sole management and control rights over the property because the applicant spouse lacks the power to encumber the assets. *See* Wis. Stat. § 766.51(1m).

Although there are no cases with respect to the effect of the Wisconsin Marital Property Act on secured credit documentation, other courts have addressed this issue. The Eighth Circuit, in an unpublished decision, affirmed a decision in which the Bankruptcy Court found there was no ECOA violation by the mortgagee. *National Bank of Commerce v. McMullan (In re McMullan)*, 196 B.R. 818 (Bankr. W.D. Ark. 1996), *aff'd*, No. 97-1086 1998 WL 382576 (June 9, 1998) (unpublished decision). Under Louisiana law, the oil and gas leases and equipment that the debtors acquired during their marriage were community

property. Thus, the ECOA was not violated when the mortgagee required the wife's signature on the notes and mortgages. Because the wife owned a co-interest in all the collateral, the lender was justified in requiring her to execute both the notes and mortgages to create a valid lien. *Id.* at 833. The court cited *In re DiPietro*, 135 B.R. 773, 777 (Bankr. E.D. Pa. 1992) (holding that bank logically required wife's signature on term note in addition to husband's signature when bank could obtain security in husband's property only by having wife be co-obligor) and *Resolution Trust Corp. v. Townsend Associates Ltd. Partnership*, 840 F. Supp. 1127, 1142 (E.D. Mich. 1993) (ruling that creditor's requiring wife's personal guarantee in addition to husband's, after his default on original loan, was not pretext for discrimination when husband and wife jointly owned assets listed on financial statements and husband did not separately own sufficient assets to be creditworthy). *McMullan*, 196 B.R. at 832.

However, in *McMullan*, the wife's signature was required on the *notes and security instruments*. The distinction between requiring signatures on notes and requiring signatures on security instruments was made clear in *Farris v. Jefferson Bank (In re Farris)*, 194 B.R. 931 (Bankr. E.D. Pa. 1996). In *Farris*, the lender was found to have violated the ECOA in requiring a spouse's signature on a note secured by a mortgage. Although the spouse's signature on the mortgage was necessary to encumber the real estate, the lender did not have a "reasonable belief" that the spouse's signature was necessary on the note to acquire the right to proceed against the real estate.

➤ **Note.** Regarding "reasonable belief," the official staff interpretation of Regulation B reads as follows:

*Need for signature-reasonable belief.* Generally, a signature to make the secured property available will only be needed on a security agreement. A creditor's reasonable belief that, to assure access to the property, the spouse's signature is needed on an instrument that imposes personal liability should be supported by a thorough review of pertinent statutory and decisional law or an opinion of the state attorney general.

12 C.F.R. pt. 202, Supp. I cmt. 7(d)(4)–2 (emphasis added).

The lender was unable to demonstrate that the spouse's signature was necessary on the note because the other spouse qualified independently as creditworthy. *Farris*, 194 B.R. at 941. In comparison, in *In re*

*DiPietro*, the spouse apparently did not qualify as independently creditworthy.

➤ **Query.** What if a note and security agreement are combined in one document? The FRB official staff commentary on section 202.7(d)(4) of Regulation B states that when a creditor uses an integrated instrument (combining the note and security agreement), the spouse may not be required to sign the integrated instrument if the signature is only needed to grant a security interest. 12 C.F.R. pt. 202, Supp. I cmt. 7(d)(4)–3. The spouse may be asked to sign an integrated instrument if the instrument makes clear that the spouse’s signature is only to grant a security interest and that signing the instrument does not impose personal liability. This disclaimer may be placed next to the spouse’s signature. *Id.*

## C. Specific Applicability of ECOA in Wisconsin [§ 5.87]

### 1. In General [§ 5.88]

In determining qualifications for credit under the ECOA, reference is to be made to state law, including provisions governing rights of management and control over property and factors that may affect the value to the creditor of the applicant’s interest in the property. *See supra* §§ 5.78–.86. As discussed in section 5.42, *supra*, the Wisconsin Marital Property Act relies in part on management and control rights with respect to credit transactions with married persons by adding to UMPA an expanded concept of management and control in connection with family-purpose credit. *See* Wis. Stat. § 766.51(1m). The Act also incorporates the UMPA approach that relies on the family-purpose doctrine to determine the extent to which marital property may be reached to satisfy credit obligations. *See supra* § 5.19.

Because of the nature of marital property in Wisconsin, the scope of management and control rights over marital property, and the fact that the basic principles of Wisconsin marital property are the same as those in community property states, Wisconsin is a “community property state” for purposes of the ECOA. *See supra* § 5.74 (FRB conclusion that Wisconsin is community property state). This conclusion is buttressed by the addition of section 766.001(2) to the Act by the 1985 Trailer Bill. That section states that “[i]t is the intent of the legislature that marital

property is a form of community property.” *See* Wis. Stat. Ann. § 766.001(2) Legis. Council Notes—1985 Act 37, § 68 (West 2009).

## **2. Applicability Based on Management and Control** **[§ 5.89]**

Section 766.51(1m) specifically provides that, in obtaining credit for a family-purpose obligation, “a spouse acting alone may manage and control all of the marital property.” This expanded application of management and control rights does not, however, extend to the excepted items of business property in section 766.70(3)(a)–(d) or to the right to encumber marital property unless, in both cases, the applicant spouse acting alone may otherwise manage and control the marital property. Wis. Stat. § 766.51(1m)(b); *see infra* § 5.25 (purchase money secured transactions). As discussed in section 5.42, *supra*, the primary purpose of section 766.51(1m) is to trigger the application of the signature or joinder rules of the ECOA to unsecured credit. *See* Wis. Stat. Ann. § 766.51(1m) Legis. Council Notes—1985 Act 37, §§ 84 to 87 (West 2009); *see also supra* §§ 5.84–.86 (ECOA signature rules). If the applicant qualifies for credit under section 766.51(1m), then the signature or joinder of the applicant’s spouse may not be requested or required under the ECOA. This analysis is similar to that for credit grantors outlined in Johnson, *supra* § 5.31, at 341.

This rule is reinforced by Regulation B, under which a creditor may not require the nonapplicant spouse’s signature, since Wisconsin law does not deny the applicant the power to manage or control marital property that the creditor must consider under the ECOA in evaluating an applicant’s creditworthiness. *See* 12 C.F.R. § 202.7(d)(3); *see also supra* § 5.85.

## **3. Applicability Based on Family-purpose Doctrine** **[§ 5.90]**

Applicability of the ECOA, although tied primarily to management and control, *see supra* §§ 5.42, .89, may also be invoked in Wisconsin under the family-purpose doctrine. Pursuant to the very broad family-purpose doctrine under the Marital Property Act, the actions of one spouse will have the effect of “obligating” marital property beyond

property that can be obligated pursuant to the rights of management and control. Viewed from the perspective of the marital property assets that can be reached to satisfy family-purpose obligations, *see supra* §§ 5.30, .31, if an obligation is within the family-purpose doctrine, all marital property assets are available. Under the ECOA, considering or applying state property laws affecting creditworthiness does not constitute discrimination. 15 U.S.C. § 1691d(b). Thus, in Wisconsin, it is permissible under the ECOA for a creditor, in evaluating creditworthiness, to consider the availability of all marital property assets to satisfy family-purpose obligations. To the extent that a creditor relies in extending credit on assets it can reach under the family-purpose doctrine, it appears that the ECOA mandates nondiscrimination in the extension of credit under that doctrine in the same way that it mandates nondiscrimination in the extension of credit under the rights of management and control.

#### **D. Joinder of Nonapplicant Spouse When Relying on That Spouse's Future Income [§ 5.91]**

##### **1. Application to Marital Property Act of ECOA Joinder Rules When Relying on Earned Income [§ 5.92]**

###### **a. Analysis Under Marital Property Act [§ 5.93]**

As discussed in section 5.85, *supra*, if an applicant for credit resides in a community property state, Regulation B permits the creditor to require the nonapplicant spouse's signature only if state law denies the applicant spouse power to manage or control sufficient community property to qualify for the credit requested and if the applicant's separate property is insufficient. 12 C.F.R. § 202.7(d)(3). When an applicant spouse is relying on future wages of the nonapplicant spouse to establish creditworthiness, is a credit grantor prohibited by Regulation B and the Wisconsin Marital Property Act from requiring joinder of the other spouse? Stated another way, in view of the provisions under the Act (such as its attribution-of-creditworthiness and special management and control provisions for credit purposes), does it constitute discrimination against the nonwage-earning spouse under the ECOA if, when he or she applies for credit, the creditor requires the signature of the nonapplicant,

wage-earning spouse before granting credit on the basis of future wage income? See Cairns, *supra* § 5.77, at 165 (similar analysis); see *supra* § 5.22.

The answer to the above question turns on the question of whether future wage income is property subject to management and control for extension-of-credit purposes under the Act. As discussed in section 5.22, *supra*, for general property law purposes, future wage income does not constitute property under the Act. However, the Act's definition of property may in fact be sufficiently broad to encompass future wages for credit-extension purposes, particularly since the Act is to be liberally construed to effectuate its purposes. See *supra* § 5.60. Further, as discussed in section 5.23–.24, *supra*, the property law definition is too limited in the context of management and control for extension-of-credit purposes. Similarly, it is too limited in the context of evaluation of creditworthiness based on the family-purpose doctrine (under which all marital property is to be considered as if it were the property of—i.e., owned by—the applicant spouse) under the Act.

According to at least one member of the UMPA drafting committee, future income is marital property that can be relied on for credit purposes under UMPA, even without Wisconsin's additional provisions: "Each spouse's wages are marital property, and because marital property is fully subject to process by postmarriage creditors of either spouse, arguably a homemaker spouse without wage income is as good a credit risk as his or her wage-earning mate." Wellman, *supra* § 5.5, at 743. Under this view, apparently the only significant risk to the creditor is if the applicant is not in fact married to the wage-earner. *Id.*

What is the effect if future wage income is not property for credit purposes under the Act? In that case, neither spouse has a property interest in the income until it is accrued or earned. Therefore, neither spouse has management and control rights over such future income, and neither spouse can use such future income in obtaining credit. See Wis. Stat. §§ 766.31, .51; see also *supra* § 5.22. Under this analysis, when granting credit to a wage-earning spouse, a credit grantor is not relying on "property." Nor is the credit grantor relying on present management and control rights over future receipts or "ownership" rights in the wage-earning spouse, whether an applicant or a nonapplicant.

Under the Act, for the purposes of obtaining and granting credit, future wage income when earned will be the property of both spouses;

the wages will not be the property of the wage-earning spouse alone. When the wages become property, both spouses will have equal ownership and equal management and control rights for the purpose of obtaining an extension of family-purpose credit under section 766.51(1m). In addition, both spouses will have equal ownership rights for credit purposes under the credit-evaluation requirements of section 766.56(1).

Regardless of whether future wage income is property subject to management and control for extension-of-credit purposes under the Act, by application of the ECOA to the Act, reliance on future wage income as a basis for determining creditworthiness must be nondiscriminatory. Under section 766.56(1), if the credit grantor places any reliance on future income—whether wage income or otherwise—the creditor must give equal weight to such income in determining creditworthiness, regardless of whether the wage-earning or nonwage-earning spouse is applying for credit. This concept operates independently of management and control, and regardless of whether future income is characterized as property, particularly since, to the extent of ownership, both parties own or will own such income since it is or will be marital property.

The credit grantor may still evaluate future wage income on objective criteria, but Regulation B requires the credit grantor to place each spouse on the same footing in the evaluation process. *See supra* § 5.83.

### **b. Analogy to Other Community Property States** **[§ 5.94]**

When considering whether the ECOA prohibits a credit grantor in Wisconsin from requiring the joinder of the nonapplicant spouse when the applicant spouse relies on the nonapplicant spouse's future wages, it may be helpful to consider how the ECOA is applied in other community property states. In many instances, the joinder issue in other community property states also has involved the question, discussed in section 5.93, *supra*, of whether future wage income of the nonapplicant spouse constitutes community property subject to management and control of the applicant spouse.

For example, one Washington commentator has implied that future wage income is, in effect, subject to management and control:

Income of either spouse is an accretion to the wealth of the community and therefore community property. Either spouse can manage and, therefore, obligate that property upon a debt. If the debt is incurred for a community purpose, the creditor can look thereafter to the community income flow of either spouse for satisfaction of the debt.

Johnson, *supra* § 5.31, at 345. This commentator further states as follows:

It is not uncommon for an applicant to seek unsecured credit in reliance on [the nonapplicant] spouse's income flow. . . . A nonapplicant spouse's income, like the applicant's income, is community property and is available to satisfy community debts. Therefore, a creditor should ordinarily treat an offer of a nonapplicant spouse's income to establish creditworthiness like any other offer of community property.

*Id.* at 346–47.

Finally, regarding joinder, this commentator concludes as follows: “In summary, the income flow of either spouse is a community asset. If either spouse's income is offered as evidence of creditworthiness for a community debt, the ECOA regulations prohibit the creditor from requiring the signature of the nonapplicant spouse.” *Id.* at 349.

A number of lawsuits in community property states involve this issue. For example, *Akulian v. American Express* (San Francisco, Cal. Sup. Ct., apparently filed Aug. 19, 1982), *noted in* Marcus A. Brown, *Update on ECOA*, 36 Pers. Fin. L. Q. Rep. 67, 68 (1982), involved a class action suit based on American Express's alleged failure to consider a husband's income that was (or would become) community property and the company's subsequent denial of issuance of a credit card to his wife. The case subsequently was dismissed by stipulation.

The same issue arose in *Clark v. Avco Financial Services*, No. 80-272 (D. Ariz., filed Apr. 10, 1980). There, an applicant spouse requested individual unsecured credit relying on community assets, including her spouse's future income, but the creditor required her husband to join to “obligate the community.” On the applicant spouse's motion for summary judgment, the court held that the creditor's policy of requiring the signature of both spouses in such an instance violated the ECOA and Regulation B, since either spouse in Arizona can bind the community (and the creditor in *Clark* had concluded that the community property



was sufficient to qualify the applicant for the loan). The court awarded punitive damages and attorney fees to the applicant spouse.

The issue of whether a nonapplicant spouse's future wage income constitutes community property subject to the applicant spouse's management and control was addressed in *United States v. ITT Consumer Financial Corp.*, 816 F.2d 487 (9th Cir. 1987), *aff'g* No. C-83-3924 JPV (N.D. Cal. 1985). In that case, filed in 1983 in the United States District Court for the Northern District of California, the United States, upon Federal Trade Commission authority, alleged that in extending credit to spouses in community property states with equal management and control (asserted, as of 1983, to be the community property states other than Texas), the defendants discriminated against married women applicants by denying individual credit when the women relied on their husbands' future income to substantiate their creditworthiness. The government further alleged that, in those states, the defendants required the husband's signature even when the applicant alone qualified for credit (because of management and control over community assets) under the defendants' standards for creditworthiness.

The district court's order, which granted the defendants' summary judgment motion, was affirmed by the Ninth Circuit Court of Appeals, which held that the defendants' practice of requiring the nonapplicant spouse to co-sign a promissory note when the applicant relied on his or her spouse's future earnings to qualify for the credit was not discriminatory under the ECOA. The court stated that the issue was a question of state law and held that, under the laws of the seven community property states involved, future earnings may not be characterized as community property until *earned*, because a circumstance such as death or divorce could cause future earnings to become separate property. *See supra* §§ 5.21–25. Hence, a married applicant's equal management power over community property in those states does not extend to the future earnings of the applicant's spouse. Therefore, a lender is justified in requiring the nonapplicant spouse's signature when reliance is placed on that spouse's future earnings to substantiate creditworthiness. *ITT*, 816 F.2d at 491.

The court also held that the defendants' co-signature requirement did not violate the ECOA or Regulation B, specifically 12 C.F.R. § 202.7(d)(1), (3), (5), because the defendants required a co-signer *only if* an applicant did not qualify individually under the defendants' standards of creditworthiness. No co-signer was required for a married applicant

unless a co-signer was also required for a similarly situated unmarried applicant. *Id.* at 493.

Because of the decision in *ITT*, the FRB amended its official staff commentary to section 202.7(d) of Regulation B with respect to signature requirements in credit transactions. *See* Equal Credit Opportunity; Update to Official Staff Commentary, 53 Fed. Reg. 11,044 (1988). The commentary was amended to read as follows:

*Reliance on income of another person—individual credit.* An applicant who requests individual credit relying on the income of another person (including a spouse in a noncommunity property state) may be required to provide the signature of the other person to make the income available to pay the debt. In community property states, the signature of a spouse may be required if the applicant relies on the spouse's separate income. If the applicant relies on the spouse's future earnings that as a matter of state law cannot be characterized as community property until earned, the creditor may require the spouse's signature, but need not do so—even if it is the creditor's practice to require the signature when an applicant relies on the future earnings of a person other than a spouse. (See § 202.6(c) on consideration of state property laws.)

### **c. Conclusion [§ 5.95]**

Under the FRB interpretation of Regulation B discussed in section 5.94, *supra*, if a spouse applies for unsecured credit based on the future earnings of the nonapplicant spouse (and the Marital Property Act applies to the spouses), the credit grantor might not be violating the ECOA by requiring the signature of the nonapplicant spouse. This rule may apply despite the fact that section 766.56(1) provides for attribution of creditworthiness between spouses. *See supra* §§ 5.52–.55. The issue under the FRB interpretation is whether the nonapplicant spouse's future earnings may be characterized under Wisconsin law as a marital property asset. *See supra* §§ 5.21–.26.

Although the *ITT* holding (that future earnings are not community property until earned, *see supra* § 5.94) was not based on Wisconsin law, the authors of this book consider it likely that the holding would be followed in Wisconsin because of the similarities in the underlying community property law principles of both the states involved and Wisconsin. Thus, in Wisconsin, under this analysis, the ECOA would

not be violated if a credit grantor required the nonapplicant spouse's signature in circumstances similar to those in *ITT*.

➤ **Note.** For a further comment on the *ITT* decision, see June M. Weisberger and H. Arleen Wolek, *WMPA and Credit: Key Changes for Creditors*, Wis. Law., Apr. 1989, at 18. The authors of that article, contrary to the position taken by the authors of this book, argue that there is reason to believe that the rationale of the *ITT* holding would *not* be followed in Wisconsin because of the Act's provisions relating to creditworthiness and those relating to a creditor's reaching assets after divorce, change of domicile, or death. See *supra* § 5.30, *infra* §§ 5.97–.104. Based on these provisions, Weisberger and Wolek conclude that, for purposes of obtaining credit, a court might decide that the future income of the nonobligated spouse is a marital property asset. Basically the same position (i.e., contrary to this book's analysis) is taken in Howard S. Erlanger and June M. Weisberger, *From Common Law Property to Community Property: Wisconsin's Marital Property Act Four Years Later*, 1990 Wis. L. Rev. 769, 788 n.74, 789. Erlanger and Weisberger base their view on the Act's special credit provisions—particularly section 766.51(1), which by its terms requires the creditor to consider future income of both spouses—and the Act's expanded collection provisions.

For a discussion of the *ITT* case and the FRB's revised official staff commentary to Regulation B, see Dan L. Nicewander, *Spousal Cosignature Rules in the Aftermath of United States v. ITT Consumer Financial Services*, 42 Consumer Fin. L.Q. Rep. 145 (1988); see also Elwin Griffith, *The Quest for Fair Credit Reporting and Equal Credit Opportunity in Consumer Transactions*, 25 Mem. St. U. L. Rev. 37, 92–94 (1994).

## **2. Application to Marital Property Act of ECOA Joinder Rules When Relying on Unearned Income [§ 5.96]**

An applicant spouse may attempt to establish creditworthiness by relying on future unearned income of the spouses, particularly income on marital property held by the nonapplicant spouse or income on nonmarital property of the nonapplicant spouse. In such an instance, the

issue—that is, whether a credit grantor is prohibited by Regulation B and the Wisconsin Marital Property Act from requiring joinder of the other spouse—is the same as when the applicant spouse is relying on future earned income of the nonapplicant spouse. The analysis discussed in sections 5.92–.95, *supra*, applies to such circumstances.

## **VIII. Practical Problems When Extending Unsecured Credit to Only One Spouse [§ 5.97]**

### **A. In General [§ 5.98]**

A major purpose of the Wisconsin Marital Property Act and Regulation B as applied to marital property is to require credit grantors to extend credit to one spouse on the basis of marital property assets or future income of the spouses. However, a number of practical problems face credit grantors in Wisconsin when both spouses are not applicants for credit. In such instances, creditors may face a diminished availability of the future income or marital property assets on which they relied in granting credit. Although family-purpose creditors subject to the Act are legally required to take all marital property income and assets into account when considering creditworthiness of married persons, creditors' access to such income and assets may be compromised or lost in some circumstances. Some of the issues of concern to creditors are described in sections 5.99–.101 and 5.104, *infra*.

### **B. Marriage Dissolution [§ 5.99]**

The existence of marital property depends on the status of the parties as married persons, and the expanded application of management and control by a nontitled spouse in family-purpose credit transactions depends on his or her status as a spouse. *See supra* § 5.37. In some community property states, spouses' separation may terminate the community or management and control rights, and hence separation is a relevant contingency for credit grantors in those states. For example, section 26.16.140 of the Washington Code provides that a spouse's wages earned while living separate and apart are separate property. Wash. Rev. Code Ann. § 26.16.140 (West, WESTLAW current with amendments received through Jan. 15, 2010). California's law has the same effect. *See* Cal. Fam. Code § 771 (West, WESTLAW current with

all 2009 Reg. Sess. laws; all 2009–2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 17 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot).

The UMPA section 1 comment explains the situation under UMPA:

[UMPA] concerns the property of married persons. If a man and a woman are not married, the property they own is *not* marital property. It may have been marital property if their marriage has been dissolved, or if one of them is deceased, but on the occurrence of such an event it loses its classification as marital property. . . . The period when certain property will be marital is during marriage and [UMPA's] provisions addressed to "spouses" will apply then as well.

Thus, to the extent a creditor has relied on the income stream of a nonobligated spouse, that income stream may be "lost" after dissolution if the creditor cannot reach it.

However, under section 766.55(2m), which governs spousal obligations, the former marital property assigned to each spouse at dissolution remains available for satisfying a family-purpose obligation to the extent of its value at the date of the decree. In addition, if the decree assigns responsibility for satisfaction of the obligation to the nonincurring spouse, "the obligation may be satisfied as if both spouses had incurred the obligation." Wis. Stat. § 766.55(2m). In the event of such an assignment, the creditor may proceed on the basis of the personal liability of each spouse. Without the personal liability of the nonapplicant spouse, which would not exist without an assignment of responsibility by the decree, the creditor's practical rights to reach assets that were formerly marital property clearly would be diminished after dissolution in the case of a family-purpose obligation. This is not the result in the case of a support obligation under section 766.55(2)(a), as to which both spouses remain obligated. See *St. Mary's Hosp. Med. Ctr. v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 706 (Ct. App. 1994) (discussed at sections 5.106, 5.110, 6.5, 6.6, 6.8, and 6.46, *infra*).

➤ **Comment.** Creditors are well advised to monitor the marital status of borrowers who have relied on marital property to establish creditworthiness. This is similar to watching for the death of borrowers. It can be argued that creditors should be able to consider the likelihood of dissolution as a factor in evaluating creditworthiness, provided the evaluation is done on a

nondiscriminatory basis. It is questionable, however, whether in evaluating creditworthiness of the nonwage-earning or nontitled applicant spouse, the creditor may take into account the effect of a possible dissolution of the marriage unless an action is pending. *See supra* §§ 5.34, .36.

At least one writer has concluded that the potential for a particular couple's divorce, if divorce is imminent, merits special attention because of the divorce's effect on the availability of the nonapplicant spouse's income:

The danger of ... divorce may sufficiently diminish the value of a nonapplicant spouse's income flow as a source of creditworthiness to permit the creditor to require the nonapplicant spouse's signature on the debt instrument.... In most other situations [that is, where there is no divorce] the ECOA will probably be interpreted to prohibit the creditor's requiring the nonapplicant spouse's signature unless the ... divorce is sufficiently certain so as to support a reasonable belief in the necessity of requiring the spouse's signature to ensure the availability of the nonapplicant spouse's income flow in the event of default.

Johnson, *supra* § 5.31, at 348.

Regulation B may allow a creditor to require a reapplication in the event of a divorce, at which time creditworthiness can be reevaluated. *See* 12 C.F.R. § 202.7(c)(2).

### **C. Change of Domicile [§ 5.100]**

Section 766.55(7) states that property available to creditors under chapter 766 remains available regardless of whether it is located in Wisconsin and regardless of whether chapter 766 no longer applies because of a change of domicile by one or both spouses. This provision was adopted to "aid creditors attempting to satisfy obligations covered by [chapter] 766 in other jurisdictions," but with an acknowledgment that "recognition of the provision may be subject to the laws of other jurisdictions." Wis. Stat. Ann. § 766.55(7) Legis. Council Notes—1985 Act 37, §§ 90 to 98 (West 2009); *see supra* § 5.38 (Act's applicability to spouses "during marriage," i.e., while both spouses are domiciled in Wisconsin); *see also infra* §§ 13.17, .22 (application of choice-of-law principles to changes in domicile).

➤ **Note.** If one or both spouses move to a common-law state, the nonapplicant spouse's future income, including future wage income, will not be classified as a marital property asset; such income may therefore be lost to the creditor as a source for repayment of the debt. As with the divorce contingency discussed in section 5.99, *supra*, it can be argued that creditors should be permitted to evaluate the change-of-domicile possibility when determining creditworthiness, provided the evaluation is done on a nondiscriminatory basis.

## D. Death [§ 5.101]

At death, as at dissolution of a marriage, marital property loses its classification as marital property. Under section 861.01, on the death of either spouse, the personal representative of the estate or other successor in interest of a deceased spouse owns the deceased spouse's undivided one-half interest in each item of former marital property as a tenant in common with the surviving spouse, who retains his or her undivided one-half interest.

Section 859.18(2), regarding satisfaction of obligations at the death of a spouse, contains the general rule that property that would have been available under section 766.55(2) to satisfy the obligation, except for the death, continues to be available, subject to a number of exceptions. The following discussion regarding the application of these exceptions is limited to those creditors who regularly extend credit and to family-purpose obligations. For a more detailed discussion of the satisfaction of obligations at the death of a spouse, see sections 12.80–.131, *infra*.

If an obligation is within the family-purpose doctrine, then on the death of the *nonobligated* spouse, that deceased spouse's marital property that is probate property remains available. *See* Wis. Stat. § 859.18(2). However, if no claim is filed in the estate of the nonobligated spouse within the time established for filing claims under section 859.01, the claim is barred against the decedent's estate. Wis. Stat. § 859.02(1). Hence, the deceased spouse's one-half interest in the former marital property that is probate property is freed from the obligation.

➤ **Caveat.** The claims of creditors who are not given notice by the personal representative of the final date for filing claims may not be barred if (1) the personal representative knew (or with reasonable

diligence should have known) of the existence of the potential claim (and the identity and mailing address of the potential claimant) and (2) the claimant did not have actual knowledge of the estate proceeding at least 30 days before the final day for filing claims. Wis. Stat. § 859.02(2)(b).

It appears that if the freed property is later distributed to the surviving spouse, it becomes available to the creditor by reason of that spouse's personal liability. *See* Wis. Stat. § 859.02(3); *see also infra* § 12.121. Regardless of whether a claim was timely filed in the estate, the former marital property and nonmarital property of the surviving obligated spouse (including any assets received from the probate estate of the deceased spouse) are available to the creditor, based on the personal liability of the surviving spouse.

Similarly, if an obligation is within the family-purpose doctrine, then on the death of the *obligated* spouse, the former marital property and the nonmarital property of the deceased obligated spouse remain obligated. Wis. Stat. § 859.18(2). This result is based on the personal liability of the obligated spouse. However, if a claim is not filed in the estate of the obligated spouse within the time established for filing claims under section 859.01, the claim is barred against the decedent's estate, with the exceptions noted in the caveat above. Wis. Stat. § 859.02(1), (3). Hence, the deceased spouse's nonmarital probate property is freed from the obligation, and his or her one-half interest in the former marital property that is probate property is freed from the obligation. *See* Wis. Stat. § 859.02(1). Under section 859.02(3), regardless of whether a claim was timely filed, the former marital property of the surviving, nonobligated, spouse remains available to the creditor subject to the exceptions in section 859.18.

The effect of section 859.18 is to enable creditors who regularly extend credit to reach the property that would have been marital property but for the spouse's death. *See* Wis. Stat. § 859.18(2). This property includes future income, even that of the surviving spouse, regardless of whether the surviving spouse is obligated. This legislative scheme recognizes the fact that creditors are required under section 766.56(1) to rely on marital property, including such future income, in extending credit. *See* Wis. Stat. Ann. § 859.18 Legis. Council Notes—1985 Act 37, § 169 (West 2002). The general exception of section 859.18(3), that the income of the nonobligated surviving spouse is not available, does not apply to an obligation resulting from an extension of credit by a



creditor who regularly extends credit. *See* Wis. Stat. § 859.18(1), (3). Similarly, the general exception, that former marital property is available only to the extent of its value at the death of the deceased obligated spouse, does not apply to an obligation resulting from an extension of credit by a creditor who regularly extends credit. *Id.*

However, in such a case—when the deceased spouse was the only obligated spouse—the following property is *not* available for satisfaction of the obligation:

1. Survivorship marital property (except as provided in subsections 766.60(5)(b) and (c), which relate to certain liens and judgment liens if execution had issued before death);
2. Joint tenancy (unless execution had issued before death on a judgment);
3. Deferred employment benefits; and
4. Life insurance (unless paid to the estate or assigned to or paid to the creditor as security).

Wis. Stat. § 859.18(4)(a).

It should be noted that simply changing marital property to survivorship marital property completely removes it from the category of property that otherwise would be available in full to satisfy the obligation. *See* Wis. Stat. § 859.18(4)(a)1. By contrast, marital property that passes to the surviving spouse by reason of a marital property agreement that operates as a will substitute under section 766.58(3)(f) remains obligated (as does marital property in other specified forms of nonprobate transfers). Wis. Stat. § 859.18(6); *see* Wis. Stat. § 859.18(5); *see also infra* § 12.82. This different treatment is based on a view of survivorship marital property as analogous to joint tenancy with right of survivorship and of property passing by a will-substitute marital property agreement as analogous to property passing under a will. *See* Wis. Stat. Ann. § 859.18 Legis. Council Notes—1985 Act 37, § 169 (West 2002).

➤ **Note.** As mentioned above, the disposition of property by a will-substitute marital property agreement on the death of a spouse does not affect the property available to a creditor to satisfy an obligation. Wis. Stat. § 859.18(6). An exception to this general rule exists,

however, if under the agreement the property was unavailable to the creditor while both spouses were alive. *Id.*; *see* Wis. Stat. Ann. § 859.18(6) Legis. Council Notes—1991 Act 301, § 35 (West 2002); *see also infra* § 7.12.

If the surviving spouse is the only obligated spouse, the following property, unless transferred to the obligated surviving spouse, is *not* available for satisfaction of the obligation:

1. Joint tenancy (unless execution on a judgment had issued before death);
2. Deferred employment benefits; and
3. Life insurance (unless paid to the estate or assigned to or paid to the creditor as security).

Wis. Stat. § 859.18(4)(b).

In sum, significant protection is provided under the probate claims procedures to creditors who regularly extend credit and who rely on the income of, and marital property assets held by, the nonobligated spouse. It appears that with respect to the contingency of death, the assets and income available to such a creditor are approximately the same as those that would have been available had the credit been extended to an unmarried person who owned all the assets (which is the standard for attribution of creditworthiness under section 766.56(1)). *See supra* §§ 5.52–.55. The primary exception is survivorship marital property, which is given traditional joint-tenancy treatment. Nonetheless, for the creditor, the contingency of the death of a married person, as compared with that of an unmarried person, requires additional monitoring, presents more complications, and may result in higher collection and other costs.

## **E. Ability to Reach Assets [§ 5.102]**

Many creditors argue that, when extending secured or unsecured credit in community property states on the basis of a spouse's management and control rights or on the basis of the family-purpose doctrine, they should not be required to consider the assets or income stream of the nonobligated spouse for repayment of the debt because as a

practical matter it may be impossible to reach such assets or income. *See* Loeb, *supra* § 5.42; Brown, *supra* § 5.42; Winnie F. Taylor, *Regulation B's Spousal Signature Rules and Community Property States: A Creditor Collection Dilemma*, ABA [Am. Bankers Ass'n] Bank Compliance, Summer 1984, at 12, 13.

In Wisconsin, however, all marital property, including the nonobligated spouse's interest in marital property, can be reached by a judgment creditor of the obligated spouse, provided that the judgment was rendered on an obligation incurred in the interest of the marriage or the family. Wis. Stat. § 766.55(2)(b). The means available may include attachment under chapter 811, garnishment under chapter 812, and levy under chapter 815. *See supra* §§ 5.30, .31; *see also infra* ch. 6.

➤ **Practice Tip.** Often, a creditor does not have (or did not seek) information about a judgment debtor's assets before granting credit. After obtaining a judgment, a creditor may serve an order to show cause on a judgment debtor pursuant to section 816.03, requiring a debtor to appear before a court commissioner. The hearing before a court commissioner is called a *supplementary examination*. In a supplementary examination, a creditor may question the debtor about all assets, including marital property assets.

## **F. Marital Property Agreements [§ 5.103]**

In general, for a marital property agreement that was executed before credit has been granted to be binding on a creditor, the creditor must have actual knowledge of it (or have been furnished a copy under certain circumstances) when the obligation was incurred. Wis. Stat. §§ 766.55(4m), .56(2)(c). Accordingly, marital property agreements executed after credit has been granted should not cause practical difficulties for creditors under the Wisconsin Marital Property Act. *See supra* §§ 5.36, .63. This is in contrast to the community property law in many other states. In those states, wage income and other assets can be reclassified (i.e., transmuted) by agreement after the debt has been incurred. Such postdebt reclassification is binding on the creditor despite the fact that it adversely affects the creditor's interest. Joan H. Henderson, *Marital Agreements and the Rights of Creditors*, 19 Idaho L. Rev. 177 (1983). This type of reclassification appears to be one of the most difficult practical problems facing creditors in other community

property states. *See* Loeb, *supra* § 5.42; Brown, *supra* § 5.42; *see also supra* § 5.81, *infra* § 7.10.

## **G. Conclusion [§ 5.104]**

Creditors' groups have argued that the Wisconsin Marital Property Act presents creditors with many practical problems. Proponents of equal access to credit argue that these considerations are a matter of "credit risk" to be considered as a part of the cost of extending credit. *See* Johnson, *supra* § 5.31, at 345–56 for a brief reference to these and related problems. Johnson states that when an unsecured creditor lends in reliance on existing community property, the creditor "impliedly accepts the risk that there will be insufficient community property to satisfy the debt upon default," and this risk does not enable the creditor to require the other spouse's signature to the debt instrument under the ECOA. *Id.* at 346. Equal access proponents also point out that these considerations are similar to those involving divorce, change of domicile, or death in common-law states. They assert that the most important consideration is the debtor's continued willingness to repay and the continued employment (and, hence, income stream) of the spouse or spouses whose wages were considered in granting the credit. It is their position that the likelihood of this income stream being interrupted or otherwise unavailable to the creditor is, as a practical matter, the same regardless of what property law applies to the spouses. Of course, it is not identical in the event of a divorce or a change in domicile, *see supra* §§ 5.99, .100, but under the policy of the Marital Property Act and the ECOA, these contingencies are not to be taken into account in extending credit to a spouse.

## **IX. Other Possible Bases for Obtaining and Granting Credit [§ 5.105]**

### **A. Duty of Support [§ 5.106]**

In Wisconsin, the duty of each spouse to support the other and to support his or her minor children is based on statutorily created personal liability. *See* Wis. Stat. § 49.90(1); *St. Mary's Hosp. Med. Ctr. v. Brody*, 186 Wis. 2d 100, 109, 519 N.W.2d 706 (Ct. App. 1993) (noting that Act modified Wisconsin's doctrine of necessities "so that it now imposes

personal liability on each spouse for the other's necessities"); *see also infra* § 5.110 (discussing *Brody*). (As explained in section 5.109, *infra*, the doctrine of necessities is based on, and coextensive with, the duty of support.) The duty of each spouse to support the other spouse is a duty owed between the spouses. Although the statutory duty of support is owed by the spouses to one another, the fulfillment of that duty through a third party's provision of necessities to one of the spouses (e.g., the provision of necessary medical treatment by a hospital) may give rise to personal liability on the part of the other spouse to the third party under the doctrine of necessities. *See Brody*, 186 Wis. 2d at 109; *see also infra* § 5.110. The duty to support a minor child is a duty of the parent owed to his or her minor children.

Section 49.90, entitled "Liability of relatives; enforcement," creates a statutory duty of support, the violation of which is a criminal act. Section 49.90(1)(a) provides that, if a dependent person is unable to maintain himself or herself, the dependent person's spouse or parent must maintain the dependent person so far as the spouse or parent is able.

Section 49.90(1m) provides that "[e]ach spouse has an equal obligation to support the other spouse" and that "[e]ach parent has an equal obligation to support his or her minor children" as provided in chapters 48 and 938. Chapter 49 provides a procedure for the district attorney to apply to the circuit court for an order to compel maintenance for a dependent person if that person's relatives fail to do so. *See Wis. Stat.* § 49.90(2). In addition, section 49.90(10) provides that, if an action under section 49.90 relates to the support or maintenance of a child, the court is to determine maintenance or support in the same manner as support is determined under section 767.511. These provisions are consistent with the intent of the Act, expressed in section 765.001(2), that marriage is a legal relationship between two equal persons "who owe to each other mutual responsibility and support."

Further, and very significantly, section 765.001(2) states as follows:

Each spouse has an equal obligation in accordance with his or her ability to contribute money or services or both which are necessary for the adequate support and maintenance of his or her minor children and of the other spouse. No spouse may be presumed primarily liable for support expenses under this section.

The measure of the duty of support and the extent of the spouses' respective responsibilities are contained in the Family Code (chapters 765–768). Section 767.501 (“Actions to compel support”) provides spouses, spouses’ minor children, persons with legal custody of spouses’ minor children, and relatives without legal responsibility for the spouses’ children a remedy to compel a spouse to provide support and maintenance to his or her spouse or minor children. The amount of the support and its apportionment between the spouses are determined by the court by reference to the factors listed in sections 767.511 and 767.56, which govern child support and maintenance payments. The factors include the comparative health of the spouses, the comparative earning capacity of the spouses, custodial responsibilities for the children, and such other factors as the court may determine are relevant.

Although a spouse who contracts for goods or services is personally liable to the creditor by contract, generally the noncontracting spouse is not personally liable to the creditor. However, when such goods or services are necessities, personal liability on the part of the noncontracting spouse may arise under the doctrine of necessities. *See Brody*, 186 Wis. 2d at 109; *see also infra* § 5.110. When an obligation to a creditor falls within the duty of support, section 766.55(2)(a) specifies the assets available to the creditor to satisfy the obligation. *See Brody*, 186 Wis. 2d at 109; *see also supra* § 5.31, *infra* §§ 6.5, .6. When an obligation to a creditor does not fall within the duty of support but constitutes a family-purpose obligation, section 766.55(2)(b) specifies the assets available to the creditor to satisfy the obligation. *See supra* § 5.31, *infra* § 6.8.

## **B. Doctrine of Necessaries [§ 5.107]**

### **1. In General [§ 5.108]**

The Wisconsin common-law doctrine of necessities, which is narrower than the family-purpose doctrine, *see supra* § 5.31, imposes personal liability on spouses for necessities furnished to the family. *See supra* § 5.106. The Act has a significant impact on the necessities doctrine. As explained in section 5.109, *infra*, the doctrine of necessities is based on and coextensive with the duty of support discussed in section 5.106, *supra*.

## 2. Status Before Act [§ 5.109]

During the period of legislative debate on predecessor bills to the Act, the Wisconsin Supreme Court redefined and reaffirmed the Wisconsin common-law doctrine of necessities in *Marshfield Clinic v. Discher*, 105 Wis. 2d 506, 314 N.W.2d 326 (1982), *Sharpe Furniture, Inc. v. Buckstaff*, 99 Wis. 2d 114, 299 N.W.2d 219 (1980), and *Stromsted v. St. Michael Hospital of Franciscan Sisters (In re Estate of Stromsted)*, 99 Wis. 2d 136, 299 N.W.2d 226 (1980). The doctrine as enunciated in those cases imposes, as a matter of public policy, a personal liability on each spouse to third parties who have provided necessities for the support of the family. This liability for payment for necessities is based on each spouse's duty of support owed to the other spouse and their minor children. The cases state that necessities include food, clothing, medicine, medical assistance, means of transportation, housing, furniture, and the like that are necessary and appropriate (based on the spouse's ability and economic and social circumstances) for the other spouse's or the children's sustenance, health, and comfort.

The Wisconsin Supreme Court held in these cases that the doctrine of necessities serves legitimate and proper purposes in today's society, including fostering and facilitating support of the family, aiding enforcement of the spousal duty of support, encouraging extension of credit to spouses (in harmony with the purposes behind the support statutes), and benefiting providers of necessities by enhancing certainty of payment. The court also held as follows:

In light of the proper function of the necessities rule in relation to the support of the family, in the absence of an express contract to the contrary, we hold that a husband incurs the primary obligation, implied as a matter of law, to assume liability for the necessities which have been procured for the sustenance of his family.

*Sharpe Furniture*, 99 Wis. 2d at 120.

The stated justifications for imposing primary liability on husbands and secondary liability on wives included the following: the fact that wives seeking credit might not have had the economic ability to make the necessary purchases, *id.* at 119; the general income-producing patterns of the contemporary family, especially the fact that wives generally had "remained behind" their husbands in the area of income production, *Stromsted*, 99 Wis. 2d at 144–45; the fact that many wives did not work

outside the home (and many others only worked outside the home on a part-time basis); and the overall fact that “wives are still far from equal with their husbands in economic resources,” *Marshfield Clinic*, 105 Wis. 2d at 515. Accordingly, the court held in *Marshfield Clinic* that the primary/secondary liability rule was the most equitable method of dividing the liability. *Id.* at 516.

Dissenting and concurring opinions in each of the three decisions vigorously challenged the concept of primary/secondary liability. These opinions emphasized that the duty of support that “underpins” the doctrine of necessities is not a hard-and-fast rule; rather, the duty is allocated between the spouses not on the basis of sex but on the basis of a number of statutory factors. *See supra* § 5.106. Accordingly, a determination would be required in each case of the apportionment of the liability between the spouses.

The Wisconsin Supreme Court’s decision that husbands are primarily liable for necessities reflects the vitality of the necessities doctrine and illustrates why the doctrine probably will continue to operate in some form, despite the adoption of the Act:

[T]he necessities rule . . . serves several important governmental objectives. The rule benefits families by making it more likely that they will obtain necessary and appropriate goods and services. It enables wives to obtain credit more easily, rather than having to depend on their husbands to make necessary purchases. It also protects wives from economic hardship by placing primary liability on husbands. This is significant because [although] wives have made substantial economic gains in the past decade . . . substantial economic disparities still persist between husbands and wives. The rule also benefits the providers of goods and services by assuring them greater certainty of payment when they extend credit to families.

*Marshfield Clinic*, 105 Wis. 2d at 510.

### **3. Status After Act [§ 5.110]**

In view of increased spousal access to credit resulting from the Act, the basis for the primary/secondary liability rule under the necessities doctrine has been greatly diminished, if not eliminated. In fact, the Act may have reduced the basis for this rule to the point that the rule could not withstand objections on constitutional or statutory grounds. *See* Wis. Stat. § 765.001(2); *Brody*, 186 Wis. 2d at 109 (concluding that section



765.001(2) has modified doctrine of necessities in Wisconsin) (discussed below); *see also Marshfield Clinic*, 105 Wis. 2d 506, 314 N.W.2d 326 (1982), and cases cited therein. *See generally* Henry J. Sommer & Margaret Dee McGarity, *Collier Family Law and the Bankruptcy Code* ¶ 3.02[2] (1991 & Supp. 2003).

The continued vitality of the doctrine of necessities and its modification by section 765.001(2) were confirmed by the Wisconsin Court of Appeals in *St. Mary's Hospital Medical Center v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 706 (Ct. App. 1994). In *Brody*, the hospital sued the former spouses for medical services rendered to the husband during the marriage. Although the divorce judgment assigned the hospital debt to the husband, the circuit court concluded, and the court of appeals agreed, that the wife also was liable to the hospital for the debt under the doctrine of necessities. The hospital appealed from the circuit court judgment, however, because that court, relying on section 766.55(2m), provided in the judgment that the hospital could satisfy the amount owed by the former wife only from marital property assets assigned to her “to the extent of the value of the marital property at the date of [the] divorce.” *Id.* at 102. Under section 766.55(2m), marital property assets assigned to each spouse under a divorce decree are available to satisfy a family-purpose obligation under section 766.55(2)(b) only to the extent of the value of the marital property assets on the date of the decree.

On appeal (in which the former wife did not participate), the court of appeals concluded that the circuit court had erred in applying the limitation on satisfaction of the judgment and that all of the former wife's assets were available to satisfy the hospital debt. Under the court's analysis, the former wife's obligation to the hospital under the doctrine of necessities fell within section 766.55(2)(a) as an “obligation to satisfy a duty of support owed to the other spouse.” *Id.* at 110. Under section 766.55(2)(a), a spouse's obligation to satisfy a duty of support owed to the other spouse may be satisfied “only from all marital property and all other property of the obligated spouse.” Because the former wife was an “obligated spouse” because of her obligation to provide support under section 765.001(2), the hospital could reach all her assets under section 766.55(2)(a). *Id.* at 111–12.

Although the court acknowledged that a support obligation will almost always involve the interests of the marriage or family, it reasoned that such an obligation must be considered as falling under section

766.55(2)(a) and not under section 766.55(2)(b) (as a family-purpose obligation) to avoid reading section 766.55(2)(a) out of the statute. By adopting this approach, the court rendered section 766.55(2m), on which the circuit court had relied in applying the limitation on collection, inapplicable to the former wife's obligation to the hospital since that subsection applies only in the case of family-purpose obligations under section 766.55(2)(b). *Id.* at 112.

With regard to the doctrine of necessities, the court stated that section 765.001(2) has modified the doctrine in Wisconsin "so that it now imposes personal liability on each spouse for the other's necessities." *Id.* at 109. The court concluded that because the spouses were married at the time the former husband incurred necessary medical expenses, the former wife was equally responsible to the hospital for the debt under section 765.001(2). *Id.*

➤ **Comment.** The court in *Brody* arguably could have reached its ultimate conclusion (i.e., that all of the former wife's assets were available to satisfy the debt to the hospital) without engaging in an analysis under section 766.55. By focusing on the fact that the former wife was *personally* liable for the debt by reason of the doctrine of necessities, analysis under section 766.55 would have been unnecessary. However, the court viewed subsection 766.55(2m) as an obstacle to the hospital's collection of the debt from the former wife, since she was the nonincurring spouse with respect to the debt and the debt arguably was a family-purpose obligation under section 766.55(2)(b). The response to this is simply that subsection (2m) is not applicable when both spouses are personally liable under the necessities doctrine, thus making further analysis under section 766.55 unnecessary.

For additional discussion of the *Brody* decision, see section 5.106, *supra*, and sections 6.5, 6.6, 6.8, and 6.44, *infra*. For additional decisions applying the doctrine of necessities following the adoption of the Marital Property Act, see *ITT Financial Services v. Graf*, No. 88-CV-574 (Wis. Cir. Ct. La Crosse County Feb. 24, 1989), and *United States v. Conn*, 645 F. Supp. 44 (E.D. Wis. 1986).

➤ **Note.** Although under the necessities doctrine a spouse is obligated to pay for the other spouse's medical expenses, it has been held that this does not permit a creditor to reach worker's

compensation benefits paid to the other spouse because of the first spouse's death or injury. Those benefits remain exempt in the other spouse's hands under section 102.27, which prohibits worker's compensation benefits from being "taken for the debts of the party entitled thereto." *See also In re Brien*, 128 B.R. 220 (Bankr. E.D. Wis. 1991).

## **X. Practical Considerations [§ 5.111]**

### **A. In General [§ 5.112]**

Many sections of this chapter refer to or discuss practical considerations and problems in connection with the system of obtaining and granting credit under the Wisconsin Marital Property Act. Those sections should be consulted first for details regarding these practical considerations. Sections 5.113–.135, *infra*, highlight some of these considerations from the viewpoint of various types of credit and offer some general conclusions.

### **B. Effect of Act on Categories of Credit [§ 5.113]**

#### **1. Commercial Credit Granted to Business Entities [§ 5.114]**

##### **a. Sole Proprietorship [§ 5.115]**

The Wisconsin Marital Property Act has significant impact on the relationship between creditors and a married sole proprietor. The considerations are basically the same as those regarding the creditworthiness of any married person. The Act affects the relationship to the extent that the sole proprietor's spouse may have incurred or will incur obligations in the interest of the marriage or the family and the creditor is relying on marital property in evaluating the sole proprietor's creditworthiness.

Accordingly, the evaluation of creditworthiness under these circumstances should include a consideration of credit obligations undertaken by the sole proprietor's spouse. For example, if the other spouse is a spendthrift or has recently filed for bankruptcy, such facts

would affect the creditworthiness of the sole proprietor. Conversely, the income of the sole proprietor's spouse becomes a consideration that may enhance the creditworthiness of the sole proprietor.

With respect to unsecured and secured credit, the assets of the sole proprietorship that are solely held by the proprietor are under the management and control of the proprietor. *See supra* §§ 5.16, .42. However, those assets, to the extent they are marital property, may be reached to satisfy an obligation incurred by the other spouse if the obligation is within the family-purpose doctrine. *See supra* § 5.31. Further, if marital property assets of the sole proprietorship are not held by either spouse (i.e., if they are untitled assets), presumably either spouse may manage and control them under the general rule of section 766.51(1)(am). *See supra* § 4.76.

### **b. Partnership [§ 5.116]**

The Marital Property Act should have no significant effect on the relationship between a partnership and creditors relying on the assets of the partnership. However, to the extent that a creditor relies on the credit of a general partner who is married, many of the considerations that apply to a sole proprietor will apply to the general partner as well. *See supra* § 5.115.

In general, it appears that the partnership's underlying assets may not be reached to satisfy a judgment based on a family-purpose obligation. However, if the partnership interest is marital property of the spouses, a family-purpose judgment creditor may be able to levy execution on the partnership interest.

### **c. Corporations and Other Entities [§ 5.117]**

The Marital Property Act should not directly affect the relationship between a corporation (or other entity, such as a trust, estate, or charitable foundation) and its creditors. The Act is relevant to credit granted to spouses, not to credit granted to separate legal entities. The marital status of a corporation's stockholders, officers, directors, or employees should be irrelevant to the creditors of the corporation. Regarding guarantees, however, see section 5.118, *infra*.

#### **d. Guarantees [§ 5.118]**

As noted in section 5.117, *supra*, marital status should be irrelevant to the creditors of a corporation. However, marital status becomes relevant when a creditor is obtaining the guarantee of a married person. The same types of considerations discussed in connection with credit extended to a sole proprietor apply. *See supra* § 5.115.

A married person's guarantee of a debt of a corporation or other entity may be within the family-purpose doctrine. The conclusive effect of a separate statement under section 766.55(1), signed by the guaranteeing spouse and stating that the obligation is being incurred in the interests of the marriage or the family, should remove the risk of a later finding of nonfamily purpose. If the guarantee is within the family-purpose doctrine, all marital property as well as the nonmarital property of the guarantor will be available to satisfy the obligation. *See supra* § 5.31. It appears that the creditor will not be justified in insisting on joinder or consent of the guarantor's spouse in connection with a loan to a business in which the spouse is an employee or an investor. *See supra* § 4.59, *infra* § 6.22.

### **2. Consumer Credit Generally [§ 5.119]**

#### **a. In General [§ 5.120]**

The approaches of financial institutions to unsecured consumer credit under the Marital Property Act are discussed in June M. Weisberger and H. Arleen Wolek, *WMPA and Credit: An Empirical Study of Financial Institutions*, Wis. Law., May 1989, at 20. The authors of that article assert that, in determining creditworthiness under the Act, some financial institutions are unduly cautious in dealing with a spouse applying for unsecured credit, while other institutions do not obtain sufficient information relating to obligations of the nonapplicant spouse. Further, the authors conclude that the practices of many financial institutions are contrary both to the legislative purposes of the credit provisions of the Act and to the provisions of the ECOA (as interpreted by the FRB in Regulation B).

### **b. Applicability of Normal Considerations of Creditworthiness [§ 5.121]**

The Marital Property Act has a profound effect on consumer credit involving married persons. This is particularly true of credit based on marital property, since both spouses can obligate marital property when family-purpose obligations are involved (in the sense of rendering such property available to the creditor for satisfaction of the obligation), and the income stream of the spouses arguably is fully available to each of them for the purpose of obtaining credit for family-purpose obligations. *See supra* §§ 5.12–.104.

### **c. Procedure for Credit Applicant [§ 5.122]**

If spouses apply for joint credit when each of them will be personally obligated, the Marital Property Act has little impact. The situation is different, however, when only one spouse applies for credit (and the other spouse will not be guaranteeing the obligation). If the nonmarital property and income stream of the applicant spouse are insufficient to justify the credit requested, the applicant spouse will rely on marital property to establish sufficient income and assets to obtain the credit requested. When an obligation within the family-purpose doctrine is being incurred, the creditor must consider all marital property. Wis. Stat. § 766.56(1). Further, when secured credit is involved, the applicant spouse will rely on marital property, based on that spouse's rights of management and control of marital property.

Depending on the type of credit being requested, the applicant spouse may be asked to supply the credit grantor with the following information, by documentation, representation, or other verification:

1. Proof of the fact of the marriage relationship;
2. A copy of any marital property agreement (if the applicant spouse intends the creditor to be bound by its terms);
3. A copy of any divorce decree, court order, or other documents (such as a unilateral statement under section 766.59 classifying income from nonmarital property as individual property) that may affect the applicant spouse's management and control rights, the classification

of property, or the obligations of the spouses (if the applicant spouse intends that the creditor be bound by them);

4. Information regarding each spouse's assets and liabilities and classification of the spouses' property;
5. Information regarding each spouse's income stream; and
6. Other credit information appropriate to the credit requested.

#### **d. Procedure for Credit Grantor [§ 5.123]**

##### **(1) Evaluation of Creditworthiness [§ 5.124]**

The credit grantor's system of evaluating creditworthiness under the Marital Property Act is similar to the system used before the Act if (1) the spouses apply jointly, (2) one spouse alone applies for credit and has sufficient individual (or other nonmarital) assets and income to support the credit, or (3) the creditor consents in writing under section 766.55(4) to look only to the assets and income of the applicant spouse. However, when one spouse alone applies for credit and must rely on marital property to establish creditworthiness, the creditor is required to follow the attribution-of-creditworthiness requirements and the procedures of the Marital Property Act. *See, e.g., supra* §§ 5.52–.55, .61–.96.

##### **(2) Verification [§ 5.125]**

The credit grantor is entitled to verify information submitted by a credit applicant and may request reasonable proof as long as it is done on a nondiscriminatory basis.

It is not clear what the credit grantor may demand to establish the marital property status of assets or the marital component of mixed property. It appears that the credit grantor may not safely rely merely on the presumption of the marital property classification under section 766.31(2), nor may the credit grantor safely rely on an affidavit of the applicant. Further, the creditor probably will not be able to obtain

information on classification of property through the normal credit-bureau reporting services.

When one spouse alone applies for credit and is relying on marital property to establish creditworthiness, it appears that the credit grantor may not insist directly on verification by the other spouse concerning information received relating to marital property, even if this requirement is applied in all cases. This follows because the other spouse has no personal relationship to the credit transaction. However, if the other spouse refuses to cooperate, the applicant spouse may have remedies available to him or her under section 766.70—for example, a claim for breach of the good-faith duty, or an order for an accounting or access, which may enable the applicant spouse to obtain necessary verification such as proof of earnings. *See infra* § 8.20. Further, it may be possible to rely on the expanded application of management and control rights in section 766.51(1m), when that section is applicable, in the spouse's attempt to obtain verification.

➤ **Query.** If the creditor is unable to obtain verification, may the credit grantor eliminate unverified assets from consideration in granting credit? If such assets are not eliminated, the credit grantor takes the risk that an asset not held by the applicant but represented as marital property may in fact be the other spouse's individual or predetermination date property. Thus, the credit grantor should be able to consider lack of verification in the evaluation process, or possibly eliminate unverified assets in the evaluation process, as long as it is done on a nondiscriminatory basis.

A credit grantor that comes within the reach of 18 U.S.C. § 1014 may choose to accept the assertions made by the applicant spouse on a credit application, relying on the deterrent against supplying false information provided by 18 U.S.C. § 1014. Under that section, it is a federal crime to knowingly make a false statement or report for purposes of influencing a wide range of federal agencies and financial institutions, including any institution whose accounts are insured by the FDIC. In addition, under section 943.39(3), anyone who, with intent to injure or defraud, “[m]akes a false written statement with knowledge that it is false and with intent that it shall ultimately appear to have been signed under oath” is guilty of a felony under Wisconsin criminal law. Therefore, a credit grantor (whether within 18 U.S.C. § 1014 or not) may choose to rely on the deterrents against providing false information by requiring that the loan application be signed under oath.



➤ **Comment.** A credit grantor may conclude that these deterrents are sufficient to prevent a credit-applicant spouse from providing inaccurate information concerning marital property. However, these deterrents may not be effective in many cases, particularly when the applicant spouse may reasonably believe that the information provided is accurate but in fact it is not.

### **(3) Either Spouse's Management and Control [§ 5.126]**

Since the exercise of management and control rights by either spouse may affect the marital property available to repay a debt, the possibility that management and control rights may have been exercised by the nonapplicant spouse is a factor creditors may consider in evaluating creditworthiness. However, a creditor may not arbitrarily reduce the creditworthiness of an applicant on this basis, since objective information can be obtained to verify the status of the other spouse's liabilities as well as the other spouse's use of marital property to obtain credit. Once obtained, this information must be used on a nondiscriminatory basis. *See supra* § 5.82.

The Marital Property Act effectively creates a system under which all marital property is available to either spouse for purposes of obtaining family-purpose credit. Under the Act, the burden is placed on the credit grantor to establish the extent to which either spouse has effectively "consumed" the creditworthiness of both spouses. The result is that an applicant spouse can obtain credit only to the extent that the total marital credit is not already committed. The Act creates what may be characterized as a "first-come, first-served" system. This system may create practical problems for applicants and for creditors as well. For example, when one spouse has an open, unused line of credit or a margin account holding securities that are marital property, that spouse may have substantially "consumed" the creditworthiness of the spouses.

➤ **Note.** If the nonapplicant spouse has not acted in good faith with respect to use of the credit resources of both spouses, the applicant spouse has remedies available under the provisions relating to breach of the good-faith duty under section 766.15 or has a right to an accounting under section 766.70(2). *See infra* §§ 8.18, .20.

#### **(4) Reliance on Family Purpose [§ 5.127]**

If the credit extended was incurred for the benefit of the marriage or the family, the obligation may be satisfied from all marital property and all other property of the incurring spouse. Wis. Stat. § 766.55(2)(b). If not, then only nonmarital property of the incurring spouse and that spouse's interest in marital property can be reached, and in that order. Wis. Stat. § 766.55(2)(d).

Unless the creditor receives a written statement of family purpose under section 766.55(1), the creditor takes a risk that unsecured credit granted to the applicant was not incurred for the benefit of the marriage or the family. However, if the written statement of family purpose is obtained at or before the time the obligation is incurred, it is conclusive evidence of that fact for the creditor. Wis. Stat. § 766.55(1). In addition, even if the statement is not obtained, the strong presumption in favor of the family-purpose doctrine, the apparent safeguards to a credit grantor following the Act's credit-granting procedures, and the policy behind the bona fide purchaser rule may protect a creditor who relied in good faith on an applicant spouse's representation of family purpose. *See infra* § 6.12.

### **3. Consumer Credit: Merchandise and Credit Cards [§ 5.128]**

The considerations, procedures, and conclusions outlined in sections 5.119–.127, *supra*, appear to apply similarly to consumer credit granted for purchases of merchandise and for consumer credit cards. However, the terms of underlying contracts relating to charge accounts, credit cards, and the like vary greatly. For example, the terms of a charge account may provide that a security interest is retained in the merchandise. This element may give the creditor some added protection and a greater likelihood of repayment by one spouse or the other. Some credit agreements also may provide that if the card is used by the nonapplicant spouse, that use constitutes an agreement to be personally liable for repayment (including, in some instances, for subsequent purchases) as if the application had originally been executed by the nonapplicant spouse. These provisions may give the creditors added protection and may serve to substantially reduce creditor concerns.

## **C. Effect of Act on Creation of Security Interest**

### **[§ 5.129]**

#### **1. In General [§ 5.130]**

The considerations outlined in sections 5.113–.128, *supra*, in connection with commercial and consumer credit generally apply to secured credit as well. The reason is that, in nearly all cases involving secured credit, evaluation of creditworthiness is the primary consideration, and reliance on the security is secondary. This is because realization on the security is expensive, time consuming, and risky (because of depreciation or fluctuation in value of the collateral). Secured credit does, however, present some additional issues under the Marital Property Act, as discussed in sections 5.131–.135, *infra*.

#### **2. A Spouse May Not Create a Security Interest in Marital Property Held by Nonapplicant Spouse**

### **[§ 5.131]**

If marital property is held by a spouse, either alone or in the alternative, or is not held by either spouse, the Marital Property Act provides that the spouse may create a security interest in the property, *see* Wis. Stat. § 766.51(1)(am), (b); *see also* Wis. Stat. § 766.01(11) (defining management and control), and the creditor may safely rely on the security instrument executed by that spouse alone. However, as explained in section 5.25, *supra*, if the spouse seeking secured credit on the basis of marital property does not hold the property (either alone or in the alternative) or if the marital property involved is not in that spouse's possession and is not held by either spouse, that spouse does not have the power to grant a security interest in the property. *See* Wis. Stat. § 766.51(1m). Accordingly, that spouse may not create a security interest in the marital property, and the creditor may not safely rely on the security instrument executed by that spouse alone. An exception exists for purchase money security interests. *See* Wis. Stat. § 766.51(1)(am); *see also supra* § 5.25.

➤ **Note.** There may be mortgages and other security instruments that purport to grant a security interest in any property “owned” by the spouse who is purporting to grant the security interest. However,

as noted above, the power to grant a security interest in marital property is based on the rules of management and control, not on ownership. The grant of a security interest in all property “owned” by the borrower is ambiguous, at best, because the borrower may grant a security interest only on the basis of management and control rights. These considerations would be particularly applicable to predetermination date documents intended for revolving collateral. *See supra* § 4.64, *infra* § 6.36.

### **3. Marital Property Subject to Management and Control by Applicant Spouse [§ 5.132]**

#### **a. Marital Property Act and Uniform Commercial Code [§ 5.133]**

The Marital Property Act, by its terms, grants an applicant spouse the legal power to pledge marital property or otherwise create a security interest in it if the property (1) is held in the applicant spouse’s name alone, (2) is not held by either spouse (but is in the applicant spouse’s possession), or (3) is held in the names of the spouses in the alternative (the “or”) form. *See* Wis. Stat. § 766.51(1)(am), (b); *see also supra* § 5.42. With respect to property governed by Wisconsin’s Uniform Commercial Code (UCC) (codified at chapters 401–409), the Marital Property Act controls over UCC provisions relating to the creation of a security interest.

The UCC previously explicitly required the signature of the debtor on a security agreement or financing statement. *See* Wis. Stat. §§ 409.203(1)(a), 402(1)(a) (1999–2000). The term *debtor* was defined to mean “the person who owes the payment or other performance of the obligation secured.” Wis. Stat. § 409.105(1)(d) (1999–2000). However, when the debtor and the owner(s) of the collateral are different, the term *debtor* means the owner(s) of the collateral. Wis. Stat. § 409.102(1)(gs). Courts have construed these requirements to mean that the signatures of all owners are required on the relevant documents to create a security interest in the collateral. *See Motz v. Central Nat’l Bank*, 456 N.E.2d 958 (Ill. 1983) (joint interests); *Casco Bank & Trust Co. v. Cloutier*, 398 A.2d 1224 (Me. 1979) (spousal co-ownership of business).

Under the Marital Property Act, marital property is “owned” by both spouses. *See* Wis. Stat. § 766.31(3). However, for purposes of the UCC, a security agreement or financing statement signed by one spouse is deemed signed by the debtor if that spouse acting alone has the right under section 766.51 to manage and control the collateral, unless a marital property agreement or court decree that is binding on the secured party under the Marital Property Act (section 766.55(4m) or 766.56(2)(c)) provides otherwise. Wis. Stat. § 409.203(4)(b). Thus, if one spouse acting alone has the right to manage and control the property, the signature of the nonincurring spouse is not required under the UCC. *See also In re Biane (Biane v. United California Bank)*, 20 B.R. 659 (9th Cir. 1982) (concluding that community property rules take precedence over UCC requirements, with result that one spouse may create security interest in community property).

With respect to creating security interests in titled marital property assets when the method for obtaining a security interest in the assets is not governed by the UCC (such as for motor vehicles), the normal management and control rules apply, regardless of the underlying marital property ownership in the nontitled spouse.

### **b. Real Estate [§ 5.134]**

In the context of a purchase money mortgage, either spouse acting alone may create the mortgage lien. *See* Wis. Stat. § 706.02(1)(f); *see also supra* § 5.25. As to existing marital real property, except for the requirement that both spouses execute conveyances of their homestead, *see* Wis. Stat. § 706.02(1)(f), if the property is held in a spouse’s name alone, it may be mortgaged by that spouse. Either spouse may mortgage such nonhomestead marital real property if it is held in the alternative (the “or”) form, although they must act together if the property is held in conjunctive (the “and”) form. *See* Wis. Stat. § 766.51; *see also supra* §§ 5.16, .17. Accordingly, problems do not appear to exist with respect to the perfection of a mortgage lien based on a mortgage of nonhomestead marital property real estate given by the record title-holding spouse (alone, or in the alternative form if the marital property classification can be established).

The expanded application of management and control rights for credit purposes does not affect these conclusions regarding real estate, since the expanded application excludes the right to create a security interest

(unless the spouse otherwise may manage and control the property), other than a purchase money security interest. *See supra* § 5.25.

#### **4. Nonmarital Property [§ 5.135]**

A spouse may solely manage and control his or her property that is not marital property. Wis. Stat. § 766.51(1)(a). Accordingly, if the asset is held or titled solely in the applicant spouse's name, the creditor receiving a security interest need not be concerned about whether the asset constitutes marital property or nonmarital property, since in either event, the applicant spouse has full rights of management and control. *See* Wis. Stat. § 766.51(1)(a), (am). However, to the extent that real estate is involved and the real estate might be or become marital property, the secured creditor (mortgage lender) needs to consider judgments against the spouse of the applicant that may constitute a lien against the real estate under section 806.15(4). Judgments against the applicant's spouse that are docketed before the recording of the mortgage may need to be considered if the real estate may constitute marital property or mixed property with a marital property component. Section 806.15(5) provides a procedure for lifting a judgment lien that has attached to real estate of the nonobligated spouse (or former spouse) of the judgment debtor when the property is exempt from execution on the lien because the real estate is not available to satisfy the underlying obligation (pursuant to section 766.55). *See also* Wis. Stat. § 815.205 (regarding certain property of spouse exempt from execution).

Since such security interests granted are effective with respect to the real or personal property involved, any later actions of the nonapplicant spouse or his or her creditors will be subject to the security interest, except, with respect to real estate, the possible lien of a judgment against the spouse of the applicant under the circumstances described in section 806.15(4). *See infra* §§ 6.51–.58 (especially 6.58), .64.

### **XI. Predetermination Date Obligations [§ 5.136]**

#### **A. In General [§ 5.137]**

With respect to creditor-debtor relationships existing before the determination date, the Wisconsin Marital Property Act by its terms does not alter the relationships between a married person (or a married couple)

and his or her (or their) creditors, if the property or obligation involved existed on the determination date. Wis. Stat. § 766.55(3). An obligation of a guarantor, surety, or indemnitor arising after the determination date under a contract executed before the determination date is classified as an obligation in existence on or before the determination date. *Id.*; *see supra* § 2.8 (determination date defined); *see also infra* §§ 6.23 (remedies of creditors with respect to predetermination date obligations), .30 (obligations not provided for under Act).

Although the creditor under a premarriage or a pre-Act obligation can reach some of the assets of the obligated spouse, Wis. Stat. § 766.55(2)(c), the Act may have a significant practical effect on the assets available to satisfy the obligation. This is because the income and marital property of the obligated spouse received or accumulated after the determination date are subject to any family-purpose obligations of the nonobligated spouse arising after the spouses' determination date. In other words, the base of assets on which the creditor originally relied may become eroded. *See infra* ch. 6.

➤ **Note.** Section 766.55(3) relates to predetermination date obligations in general—that is, to obligations in existence (1) before marriage, (2) before establishment of both spouses' domicile in Wisconsin (after the effective date of the Act), or (3) before the effective date of the Act (for spouses who are both domiciled in Wisconsin on the effective date of the Act). *See* Wis. Stat. § 766.01(5) (definition of determination date). However, the specific section dealing with creditors' recovery for such obligations—section 766.55(2)(c)1., 2.—relates only to obligations in existence before marriage or before the effective date of the Act. *See infra* § 5.138.

In contrast, there is no specific section dealing with recovery by a creditor of an obligation in existence before the establishment of the spouses' domicile in Wisconsin after the effective date of the Act. Arguably, such obligations should be treated no differently than obligations arising before marriage or before the effective date of the Act for spouses who are both domiciled in Wisconsin on the effective date of the Act. However, in the absence of a specific statutory section comparable to section 766.55(2)(c)1. and 2., a creditor's recovery for an obligation in existence before the establishment of the spouses' domicile in Wisconsin after the effective date of the Act is available without reference to categories of obligation under the Act. *See infra* § 6.30.

## **B. Obligations Existing Before Marriage or Before Act's Effective Date [§ 5.138]**

With respect to a spouse's obligation attributable to an obligation that arose before marriage or before January 1, 1986, for spouses whose determination date is the effective date of the Act, neither the creditor's interest nor the debtor's interest appears to be adversely affected in any significant way by the marriage or the Act. The Act attempts to leave the parties where they would have been absent the marriage or absent the Act. This is accomplished by providing that the obligation may be satisfied from nonmarital property of the obligated spouse and from that part of the marital property that would have been the property of that spouse but for the marriage or the enactment of the Act. *See Wis. Stat. § 766.55(2)(c)1., 2.; see also infra § 6.23.*

However, as noted in section 5.137, *supra*, the base of assets upon which the creditor has relied may become eroded by reason of the application of section 766.55(2) to obligations incurred after the determination date.



# Marital Property Law in Wisconsin

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Volume II

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## **I. Scope of Chapter [§ 6.1]**

The creation of the debtor-creditor relationship is discussed in chapter 5, *supra*. Among the considerations involved are how various types of obligations may be incurred and which assets are available for satisfaction. *See supra* ch. 5.<sup>1</sup>

This chapter discusses the process of enforcement of obligations by creditors, including creditors' rights based on the category of obligation; certain acts by creditors and debtors that may enlarge or reduce the creditor's right or ability to recover; collection procedures; debtors' rights; and bankruptcy.

## **II. Categories of Obligations and Recovery Available [§ 6.2]**

### **A. In General [§ 6.3]**

Sections 6.4–.31, *infra*, set forth how the purpose and circumstances surrounding a transaction or event determine the category of the obligation incurred by a spouse. The category of obligation then determines which classifications of property of the spouses may be involuntarily recovered by a creditor to satisfy the obligation.

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189; all references to the United States Code (U.S.C.) are current through Public Law No. 111-156 (excluding Pub. L. Nos. 111-148 and 111-152) (Apr. 7, 2010); all references to the Wisconsin Administrative Code are current through Wisconsin Administrative Register, No. 652 (Apr. 14, 2010) (eff. Apr. 15, 2010); and all references to the Treasury regulations are current through 75 Fed. Reg. 18,375 (Apr. 9, 2010). Textual references to the Wisconsin Statutes are hereinafter indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

## **B. Obligation for Support; Doctrine of Necessaries**

### **[§ 6.4]**

#### **1. Support [§ 6.5]**

Under the Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or the Wisconsin Marital Property Act], a married person's obligation for the support of his or her spouse or minor children may be satisfied from all marital property and all other property of the obligated spouse, including his or her individual and predetermination date property. Wis. Stat. § 766.55(2)(a). Section 765.001(2) states that the obligation is equal between the spouses but defines this equality in terms of each spouse's relative ability to provide goods and services. *See supra* §§ 5.30 (regarding whether personal liability is imposed in Wisconsin for support obligations), 5.31; *see also infra* ch. 11.

Under *St. Mary's Hospital Medical Center v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 706 (Ct. App. 1994), a creditor who provides necessary goods and services to one spouse may have a direct cause of action against the other spouse under the doctrine of necessities. The imposition of this doctrine results in personal liability of the nonincurring spouse and categorization of the obligation as a support obligation under section 766.55(2)(a).

*Brody* concerned responsibility for medical expenses the husband had incurred before the spouses' marriage was dissolved. The dissolution decree assigned the obligation to pay these expenses to the husband. *Id.* at 103; *see* Wis. Stat. § 766.55(2m). When the expenses remained unpaid, the hospital sued both former spouses. The circuit court held that the former wife was personally liable for the full amount of the expenses under the common law doctrine of necessities; this portion of the judgment was not appealed. Since the former wife was not assigned the obligation by the dissolution decree, however, the circuit court held that under section 766.55(2m) her assets were available only to the extent of the value of marital property assets she received pursuant to the decree. The circuit court's application of section 766.55(2m) also resulted in her income not being subject to recovery.

The court of appeals reversed the portion of the judgment that restricted recovery of the former wife's assets to the marital property assets she had received at dissolution to the extent of their value at dissolution. The appeals court held that the common law doctrine of necessities continues to be viable after the enactment of Wisconsin's marital property laws and that its application results in personal liability of each spouse for the full amount of the obligation. *Brody*, 186 Wis. 2d at 109. However, section 765.001(2) removes the primary obligation of the husband and secondary obligation of the wife, making the spouses equally liable.

The former wife's liability for medical services furnished to her former husband arose under the common law, not under marital property laws. The finding that the former wife had personal liability might therefore have ended the controversy because all of a person's nonexempt assets are available to satisfy his or her obligations. The creditor had brought the action against both spouses after they were no longer married, and the satisfaction of obligations under section 766.55(2)(a) or (b) applies only to married persons. However, because the obligation to the hospital was incurred by the former husband during marriage, the dissolution decree assigned that obligation to the husband, and the circuit court had applied section 766.55(2m), the court chose to address the category of obligation under section 766.55(2) and the effect of section 766.55(2m) on the assignment.

Although necessary obligations would always be in the interest of the marriage or the family, the court characterized these obligations as for the support of a spouse under section 766.55(2)(a), not as family-purpose obligations under section 766.55(2)(b). The court stated that the presumption of family purpose under section 766.55(1) applies to obligations "incurred" by a spouse, and the wife in this case did not incur the obligation, even though she was personally liable for it. Therefore, the presumption of family purpose was not applied as to her. Furthermore, section 766.55(2)(b) refers to obligations "incurred" by a spouse, whereas section 766.55(2)(a) refers to the "obligated" spouse. Here the wife was "obligated" under the doctrine of necessities but was not the "incurring" spouse. Thus, section 766.55(2m), which limits recovery to marital property assets that were received by a nonincurring former spouse who was not assigned the obligation in the dissolution decree, to the extent of the assets' value at dissolution, and which applies only to family-purpose obligations under section 766.55(2)(b), would not apply to support obligations under section 766.55(2)(a). The court

reasoned that categorizing obligations for necessities under section 766.55(2)(b), as the circuit court had done, would “read the support category out of the statute through disuse.” *Id.* at 111. The court also observed that providing the widest possible recovery by creditors through section 766.55(2)(a) enhances the availability of necessities and provides a support function for the spouse receiving the necessary goods and services. *Id.* at 112.

While the relative ability of a spouse to provide support for the other spouse and for their minor children under section 765.001(2) may be relevant to obligations owed to each other, and to rights of contribution between spouses, it does not apply to the spouses’ obligations to creditors. The doctrine of necessities results in personal liability for the entire amount.

The dissent in *Brody* pointed out that each spouse is only obligated for support obligations to the extent of his or her ability to provide support, and that the majority made no finding as to the relative abilities of the defendant former spouses to provide support for each other. Therefore, the dissent would have limited recovery to assets available under section 766.55(2m). *See also supra* § 5.110.

Cases decided after *Brody* have reaffirmed the principle that both spouses are personally liable for medical services provided either spouse and that section 766.55(2)(a) describes the classification of property available for recovery. *See Sinai Samaritan Med. Ctr., Inc. v. McCabe*, 197 Wis. 2d 709, 541 N.W.2d 190 (Ct. App. 1995); *Froedtert Mem’l Lutheran Hosp., Inc. v. Mueller*, No. 95-1449, 1996 WL 250835 (Wis. Ct. App. May 14, 1996) (unpublished opinion not citable per section 809.23(3)); *see also Dean Med. Ctr., S.C. v. Conners*, 2000 WI App 202, 238 Wis. 2d 636, 618 N.W.2d 194 (holding that creditor could sue both parents for entire amount due under doctrine of necessity, notwithstanding paternity judgment that established each parent responsible for one-half of child’s medical expenses).

In addition to the right of one spouse (or that spouse’s creditor) to recover from the other spouse for specific obligations, each spouse is entitled to support in general from the other spouse. The amount of the general support obligation is set under section 767.501. *See infra* § 11.31. In determining the spouses’ respective obligations, the court applies considerations listed in sections 767.511 and 767.56 (concerning child support and maintenance, respectively). A decree under section

767.501 puts spouses who are still married (but probably separated) in the same economic position as former spouses to whom an order for support under sections 767.511 and 767.56 applies. *But see infra* § 9.5 (income tax consequences for spouses living apart).

## 2. Necessaries [§ 6.6]

The common law doctrine of necessities is a creditor's remedy. In Wisconsin before January 1, 1986, the effect of the doctrine was to impose primary liability on the husband to creditors who provided necessary goods and services to the wife and children regardless of which spouse entered into a contract with the creditor. If the husband was unable to satisfy the obligation, secondary liability was imposed on the wife. *See Marshfield Clinic v. Discher*, 105 Wis.2d 506, 314 N.W.2d 326 (1982); *Sharpe Furniture, Inc. v. Buckstaff*, 99 Wis. 2d 114, 299 N.W.2d 219 (1980); *Stromsted v. St. Michael Hosp. of Franciscan Sisters (In re Estate of Stromsted)*, 99 Wis. 2d 136, 299 N.W.2d 226 (1980); *see also United States v. Conn*, 645 F. Supp. 44 (E.D. Wis. 1986) (holding that attorney fees for criminal defense are necessities); *supra* § 5.109.

The necessities doctrine was harmonized with the Marital Property Act in *St. Mary's Hospital Medical Center*, 186 Wis. 2d 100, in which the court held that medical services fall within the common law doctrine of necessities for which both spouses are personally liable and that the obligation is categorized as a support obligation under section 766.55(2)(a). *See supra* §§ 5.37, 6.5; *see also Sinai Samaritan Med. Ctr.*, 197 Wis. 2d 709 (holding that obligation under doctrine of necessities arises under section 765.001, not chapter 766); *Froedtert Mem'l Lutheran Hosp.*, No. 95-1449, 1996 WL 250835 (Wis. Ct. App. May 14, 1996) ("In summary, the doctrine of necessities, as modified by section 765.001(2), Stats., imposes liability upon Mrs. Mueller; section 766.55(2)(a), Stats., describes what property may be reached; and section 803.045, Stats., clarifies the procedure when a creditor may commence an action to satisfy a judgment"); *Medical Bus. Assocs. v. Steiner*, 588 N.Y.S.2d 890 (App. Div. 1992) (discussing evolution of common law doctrine of necessities; under New York law, incurring spouse is held primarily liable, and other spouse's liability requires finding as to each spouse's ability to pay and whether provider relied on nonincurring spouse's creditworthiness); Sallie L. Rubenzer, *Necessaries and Family Purpose Debts*, Wis. Law., Oct. 1996, at 14; Jay M. Zitter, Annotation,

*Modern Status of Rule That Husband Is Primarily or Solely Liable for Necessaries Furnished Wife*, 20 A.L.R.4th 196 (1992). See also Henry J. Sommer & Margaret Dee McGarity, *Collier Family Law and the Bankruptcy Code* ¶ 3.03[2][b] (1991, Supp. Ann.).

## **C. Obligations Incurred in Interest of Marriage or Family [§ 6.7]**

### **1. In General [§ 6.8]**

Although it would appear that any obligation for necessities would fall within the category of obligations in the interest of the marriage or the family, the court in *St. Mary's Hospital Medical Center*, 186 Wis. 2d 100, found otherwise. The court held that medical services fall within the common law doctrine of necessities for which both spouses are personally liable and that the obligation is categorized as a support obligation under section 766.55(2)(a). *Id.* at 111–12; see *supra* §§ 5.37, 6.5; see also *Dean Med. Ctr., S.C. v. Conners*, 2000 WI App 202, 238 Wis. 2d 636, 618 N.W.2d 194 (holding that creditor could sue both parents for entire amount due under doctrine of necessities, notwithstanding paternity judgment that established each parent responsible for one-half of child's medical expenses).

Most other nontort obligations of either spouse incurred during marriage—whether incurred by contract, penalty, fine, or any other manner—are incurred in the interest of the marriage or the family, and creditors to whom these obligations are due may recover pursuant to section 766.55(2)(b). That section provides that obligations incurred in the interest of the marriage or the family may be satisfied from all marital property held by either or both of the spouses and from the individual and predetermination date property of the incurring spouse. Wis. Stat. § 766.55(2)(b). On the basis of the incurring spouse's personal liability, any creditor may recover from that spouse's nonmarital property.

➤ **Comment.** Section 766.55(2)(b) enlarges the pool of assets available to satisfy family-purpose obligations by making available marital property held by the incurring spouse, the nonincurring spouse, or both. Other community property states having a similar

rule allowing recovery of community property for most obligations of spouses sometimes refer to this as the *family-purpose doctrine*.

To be a family-purpose obligation, an obligation must have been incurred *during marriage*, Wis. Stat. § 766.55(1), defined as the period in which both spouses are domiciled in Wisconsin between the determination date and the termination of the marriage at dissolution or death, Wis. Stat. § 766.01(8). *See supra* § 2.8 (discussion of concept during marriage).

Whether a family purpose exists in connection with incurring an obligation is a question of fact. There is a presumption that all obligations are incurred in the interest of the marriage or the family. Wis. Stat. § 766.55(1); *Schmidt v. Waukesha State Bank*, 204 Wis. 2d 426, 442–43, 555 N.W.2d 655 (Ct. App. 1996); *see supra* §§ 5.31, .32. A person attempting to rebut the presumption of family purpose has the burden of proving that the nonexistence of the family purpose is more probable than its existence. Wis. Stat. § 903.01; *Schmidt*, 204 Wis. 2d at 443. If either spouse is able to rebut the presumption of family purpose, only the incurring spouse's individual and predetermination date property and that spouse's interest in marital property, in that order, may be reached. Wis. Stat. § 766.55(2)(d); *see also infra* §§ 6.29, .51–.58. This rule protects the nonincurring spouse's individual and predetermination date property and his or her interest in the marital property from recovery by the incurring spouse's nonfamily-purpose creditors.

Notwithstanding the actual purpose of an obligation, if the incurring spouse has, before the obligation is incurred, signed a separate statement that the obligation is or will be in the interest of the marriage or the family, that statement is conclusive evidence that the obligation is a family-purpose obligation. Wis. Stat. § 766.55(1); *Bank One, Appleton, NA v. Reynolds*, 176 Wis. 2d 218, 500 N.W.2d 337 (Ct. App. 1993).

➤ **Note.** A family-purpose statement is conclusive as to the classification of assets the creditor may recover, but it does not prevent the nonincurring spouse from recovering from the other spouse under section 766.70 if the obligation was not actually a family-purpose obligation. Wis. Stat. § 766.55(1); *see infra* § 8.36.

A spouse's right to manage and control a specific asset classified as marital property does not determine whether a creditor may recover that

asset to satisfy a family-purpose obligation incurred by the spouse. Section 766.51(1m) grants each spouse management and control of all marital property when applying for an extension of credit, with certain exceptions relating to marital property used in a business in which the other spouse is active. These exceptions are described in section 766.70(3)(a)–(d) and include partnerships and joint ventures in which the nonincurring spouse is a general partner or participant, limited liability company interests held by the other spouse as a member, professional corporations, sole proprietorships, and corporations that are not publicly traded. *See supra* §§ 4.6, 5.39. Even though management rights in these marital property business assets are restricted, the excepted marital property assets are nevertheless available to the creditor of a family-purpose obligation. Wis. Stat. § 766.55(2)(b); *see also* Wis. Stat. § 706.02(1)(f) (joinder required for conveyance of homestead property except for purchase money mortgage).

The issue of whether an obligation is or is not a family-purpose obligation can arise in an initial proceeding to enforce a debt. *See infra* §§ 6.51–.58. If the issue is not determined in the initial proceeding, it may arise in postjudgment proceedings involving the attempted recovery of marital property assets to satisfy the judgment. *See infra* §§ 6.59–.62.

➤ **Note on Terminology.** Actions affecting one spouse’s interest in a marital property asset when that spouse’s personal liability has not been established have sometimes been called actions in rem or actions quasi in rem. This is a misnomer. Actions in rem involve adjudication of the rights of all the world in a particular asset. The asset itself is the defendant, and the determination of its status or disposition is the outcome of the action. *See* 1 Am. Jur. 2d *Actions* § 40, at 573 (1962); *Pennoyer v. Neff*, 95 U.S. 714 (1877). Proceedings quasi in rem determine the rights of particular persons in a particular asset. An action to reach and dispose of a particular asset to satisfy a debt is quasi in rem. 1 Am. Jur. 2d *Actions* § 41, at 574 (1962); *see* Wis. Stat. § 801.07. In contrast, a family-purpose obligation for which only one spouse is personally liable subjects assets of a particular *classification* to recovery but does not necessarily subject a particular *asset* to recovery.



## 2. Analogy to Other Community Property States

### [§ 6.9]

Case law in states that have developed the family-purpose doctrine—Washington, Arizona, and New Mexico—may sometimes be helpful in analyzing policies and issues relevant to a family-purpose determination. *See* Unif. Marital Property Act § 8 cmt. The Uniform Marital Property Act (UMPA) is reprinted in appendix A, *infra*. Care must be taken, however, to compare the underlying rule governing property available for recovery at the time the case was decided. If the rule was that only separate property, and no community property, was available to satisfy a nonfamily-purpose (separate) obligation, then the court may have strained to find a family purpose to reach an equitable result. Such a finding would allow recovery in a case in which the defendant owned no separate property. For example, in *LaFramboise v. Schmidt*, 254 P.2d 485 (Wash. 1953), the defendant husband had taken “indecent liberties” with the six-year-old plaintiff. The court found a community obligation because the defendant and his wife were at the time acting as paid babysitters—that is, performing a commercial endeavor intended to benefit the community. If the court had found that the injury was a separate obligation, the child would probably have received nothing, although this is not stated in the case.

In addition to the fact that cases may be affected by issues extraneous to a family-purpose determination, it appears that most reported cases interpreting the family-purpose doctrine in community property states arise in a tort context. This may not be analogous to situations in which the issue arises in a commercial context in Wisconsin. The Wisconsin Act has a specific rule for torts incurred during marriage that does not require a family-purpose analysis. Wis. Stat. § 766.55(2)(cm); *see infra* §§ 6.26–.28. Cases in these other jurisdictions may be helpful, however, in analyzing general policies and principles related to the family-purpose doctrine.

It appears from case law in other community property states employing the family-purpose doctrine that it is not necessary for the obligation to benefit the spouse or family to support a finding of family purpose. *See* Harry M. Cross, *The Community Property Law in Washington (Revised 1985)*, 61 Wash. L. Rev. 13 (1986); Keith D. Ross, *Sharing Debts: Creditors and Debtors Under the Uniform Marital Property Act*, 69 Minn. L. Rev. 111 (1984). *See also* *Washington*

*Community Property Deskbook* 6-40 to 6-45 (George T. Shields et al. eds., Wash. State Bar Ass'n 2d ed. 1989) [hereinafter *Washington Deskbook*]. The facts and circumstances of each case determine whether a family purpose existed when the obligation arose, regardless of whether a benefit resulted. Moreover, the activity may be characterized as having a family purpose regardless of whether the nonincurring spouse opposed the action.

Again by analogy to other community property states having the family-purpose doctrine, if the nonincurring spouse ratifies the obligation, it may be possible, under the doctrine of estoppel, for one spouse to obligate marital property even though no family purpose exists. In Washington, for example, an agreement for support by the putative father of children born of an extramarital relationship was found to have been ratified by his wife. *See Peterson v. Eritsland*, 419 P.2d 332 (Wash. 1966). The wife was fully aware of the situation, did not repudiate the agreement, wrote several checks to carry out the agreement, and signed several joint income tax returns claiming the children as dependents. Under these circumstances, the court refused to allow the wife to claim a nonfamily purpose to shield one-half of the community assets. *Id.*

In contrast to Wisconsin, five community property states (California, Nevada, Idaho, Texas, and Louisiana) allow recovery from community property only to the extent that a spouse has management and control of that property. This is known as the managerial system. *See, e.g., In re Nahat*, 278 B.R. 108 (Bankr. N.D. Tex. 2002) (holding that earned income is “special” community property under Texas law because only the earning spouse has management and control, and earnings are not subject to claims against the other spouse). Case law in these states would therefore be of little or no assistance in interpreting liability based on the family-purpose doctrine under the Wisconsin Act. *See also supra* ch. 5 (extension of credit).

### 3. Commercial and Other Contractual Obligations [§ 6.10]

#### a. Commercial Transactions [§ 6.11]

The family-purpose doctrine applies to nontort obligations incurred during marriage in both commercial and noncommercial settings. *See* Wis. Stat. § 766.01(8). Section 766.55(2)(b) provides that an obligation incurred in the interest of the marriage or the family may be satisfied only from all marital property assets and from all nonmarital property assets of the incurring spouse. A creditor may bring an action to recover under this section against the obligated spouse, the incurring spouse, or both spouses. Wis. Stat. § 803.045(1). If the creditor cannot obtain jurisdiction over the obligated or incurring spouse, the creditor may proceed against the nonobligated or nonincurring spouse. Wis. Stat. § 803.045(2); *see infra* §§ 6.52–.54; *see also* Wis. Stat. § 766.01(2r) (instances in which definition of creditor refers only to persons or entities that regularly extend credit). After a creditor obtains judgment, it may proceed against either spouse to recover marital property. Wis. Stat. § 803.045(3); *see infra* §§ 6.59–.62.

➤ **Comment.** Creditors that operate in a commercial setting and deal with the general public, such as banks and merchants, are less likely than creditors that do not ordinarily extend credit to be personally acquainted with the borrower. They are, therefore, less likely to be able to accurately discern the purpose for which the obligation is incurred. A commercial creditor deals with a larger volume of credit than a person who is not in the business of extending credit, and this reduces the likelihood that the commercial creditor will know how funds acquired in a credit transaction will be put to use. Since a spouse may manage all marital property (with certain exceptions) to obtain an extension of credit for what is ostensibly a family-purpose obligation, it would not be fair if the creditor could recover from only half of the marital property if the obligation were later found not to be in the interest of the marriage or the family. *See* Wis. Stat. § 766.55(2)(d); *see also infra* § 6.29. The Act prevents this result.

Even though a creditor in the business of extending credit may have no practical way of determining the borrower's purpose, the system of

satisfying obligations under the Act provides a number of protections for such creditors:

1. The presumption of family purpose, which shifts the burden to the borrower or his or her spouse to prove otherwise, provides an advantage to the creditor seeking to recover marital property assets to satisfy the debt. Wis. Stat. §§ 766.55(1), 903.01.
2. Any creditor, not just a creditor in the business of granting credit, may request a separate family-purpose statement signed by the incurring spouse at or before the time the obligation is incurred. Wis. Stat. § 766.55(1). This statement recites that the obligation is or will be incurred in the interest of the marriage or the family. Such a statement is conclusive evidence as to the creditor that a family-purpose obligation exists. *Id.*; see *Bank One, Appleton, NA*, 176 Wis. 2d at 220–21; *Park Bank-West v. Mueller*, 151 Wis. 2d 476, 484, 444 N.W.2d 754 (Ct. App. 1989); see also *supra* § 5.71.

➤ **Comment.** A signed statement prevents family purpose from becoming an issue in the collection proceedings, but it does not affect any interspousal remedy relating to the improper signing of the statement. See *supra* § 5.71, *infra* §§ 8.18, .36. It appears that most commercial lenders include such a statement with loan applications or have a separate statement signed if they do not use written applications. See Howard S. Erlanger & June M. Weisberger, *From Common Law Property to Community Property: Wisconsin's Marital Property Act Four Years Later*, 1990 Wis. L. Rev. 769. The effect of the separate family-purpose statement is not clear if a creditor has actual knowledge of a nonfamily purpose. The statement appears to be conclusive in all circumstances, but estoppel based on fraud or collusion may be appropriate if such knowledge can be proved.

3. If the creditor meets the requirements of a bona fide purchaser under section 766.57, the creditor is unaffected by any claims the spouses may have against each other. See *supra* § 5.28. Actual knowledge of a nonfamily purpose may deny bona fide purchaser protection to a creditor. Wis. Stat. § 766.57(1)(a). (See section 5.28, *supra*, for a discussion of section 766.57 as it relates to secured and unsecured creditors.)

The Act makes no distinction between initial extensions of credit and renewals of existing credit. A renewal is usually regarded as an additional extension of credit. This might be important if a credit relationship was in place before the spouses' determination date and it is renewed thereafter. Since the Act was not intended to alter a spouse's existing relationships with creditors, it would be anomalous to allow a spouse to convert a predetermination date obligation into a family-purpose obligation, with creditors' expanded rights of recovery, by simply renewing the obligation. *See* Wis. Stat. § 766.55(3). However, the granting of additional credit or other modification of terms, thus creating an entirely new transaction, may under some circumstances convert a predetermination date obligation to one incurred after the determination date.

Guarantees entered into before the determination date and enforced thereafter are treated as predetermination date obligations. Wis. Stat. § 766.55(3); *see infra* § 6.22.

In *Mitchell Bank v. Schanke*, 2004 WI 13, 268 Wis.2d 571, 676 N.W.2d 849, the Wisconsin Supreme Court, reversing the court of appeals, held that a dragnet clause in a mortgage signed by both spouses was both enforceable and sufficient to secure debts incurred only by the husband. There was no evidence that the husband's debts were other than family-purpose debts. Thus, marital property of both spouses was recoverable for these debts, and this satisfied the requirement in the dragnet clause that the mortgage secured future joint debts.

## **b. Incidental Credit Transactions [§ 6.12]**

The debt satisfaction system under the Act, based on the classification of property available to satisfy the various categories of obligations, applies to all creditors. *See* Wis. Stat. § 766.55(2). The definition of the term creditor under section 766.01(2r) limits applicability of certain parts of the Act to those who regularly extend credit, but section 766.55(2) is not so limited. *See* Wis. Stat. § 766.01(2r); *see also supra* § 5.46.

The incidental creditor who is not in the business of extending credit is not required to consider property available to satisfy the obligation in determining creditworthiness. Presumably, such a creditor will in many cases use criteria that are not collection-oriented, such as family relationships, in determining whether to extend credit to a particular

debtor. The incidental creditor may also be in a better position to evaluate whether the obligation is incurred in the interest of the marriage or the family.

In addition, incidental creditors are entitled to the expanded pool of assets available to family-purpose creditors in that such obligations are presumed to be incurred in the interest of the marriage or the family. Wis. Stat. § 766.55(1). A separately signed statement of family purpose is conclusive evidence of such a purpose. *Id.*

#### **4. Tax Liability [§ 6.13]**

##### **a. Tax on Spouses' Income [§ 6.14]**

###### **(1) Reporting Requirements [§ 6.15]**

Income from marital and nonmarital property assets held or owned by either spouse is classified as marital property unless a marital property agreement under section 766.58, a unilateral statement under section 766.59, a court order under section 766.70, or another means of reclassifying assets alters this classification. Wis. Stat. § 766.31(4), (7p), (10). Income earned by either spouse is likewise classified as marital property unless a marital property agreement under section 766.58, another similar agreement, or a court order under section 766.70 provides otherwise. Wis. Stat. § 766.31(4), (7p), (10). Consequently, each spouse owns as marital property an undivided one-half interest in such income and is subject to Wisconsin and federal tax reporting requirements on that one-half interest in income. Distributions to a spouse from a trust created by a third party and income from assets received as a gift from the donee's spouse, unless the donor provides otherwise, are the donee spouse's individual property. Wis. Stat. § 766.31(7)(a), (10).

If spouses file a joint return, the spouses' marital property income and the individual property income of each spouse are reported on the return. A spouse filing a separate return reports one-half the income classified as marital property and all of that spouse's income classified as individual property. The filing of separate returns by separated spouses creates special problems for the spouse who owns a one-half interest in the income classified as marital property received by the other spouse but who is unable, because of lack of information, to report such income or

is unable to obtain access to the funds necessary to pay tax on that portion.

Section 71.10(6)(b) incorporates and expands the innocent-spouse provisions of I.R.C. § 66(c) for spouses filing separate returns. Similarly, section 71.10(6)(a) incorporates the innocent-spouse protections of I.R.C. § 6015(a) to (d) and (f) for failure to report or for underreporting of either marital property income or individual property income of one spouse on a joint return. Section 71.10(6m) applies these protections to former spouses. These problems and available protections are discussed in chapter 9, *infra*; see also chapter 12, *infra*, for discussion of the collection of Wisconsin income taxes after the death of a spouse.

A taxpayer's spouse or former spouse who might be liable or whose property might be recoverable for tax due or assessed on the taxpayer's return is entitled to information on the return. Wis. Stat. § 71.78(4)(k); *see also* chapter 9, *infra*.

## **(2) Recovery of Federal Taxes [§ 6.16]**

If spouses file state and federal joint income tax returns, both spouses are personally liable for the entire amount of tax due, even though some of the income reported may be classified as individual property. Therefore, all classifications of property of both spouses may be recovered to satisfy the joint income tax obligation.

If spouses file separate returns, only the spouse signing the return is personally liable for the tax. The extent of the community property that may be recovered to satisfy a federal tax obligation for which only one spouse is personally liable is indicated by cases involving:

1. The recovery of community property or marital property generated by the nonliable spouse, for premarriage and pre-effective date federal tax obligations of the other spouse; and
2. The recovery of certain types of assets from nonliable spouses (e.g., life insurance beneficiaries).

Cases addressing premarriage and pre-effective date federal tax obligations indicate that collection of the federal tax owed depends on federal rules that take advantage of the concept of community property

ownership and on the rights of creditors under state law. *Medaris v. United States*, 884 F.2d 832 (5th Cir. 1989), involved a federal tax obligation incurred by a spouse before marriage. In that case, only the husband was liable for federal taxes incurred before the marriage. Under the Texas statute relating to the satisfaction of liabilities, a creditor could reach the husband's entire income for his premarriage debts. His wife's income was not subject to recovery for the debts under state law, even though her income was community property. The IRS gave notice of levy to the husband, but not to the wife, and proceeded to levy on all his income and one-half her income. The district court found that one-half of the wife's income and only one-half of the husband's income could be recovered to satisfy the husband's tax liability and also found that the wife was not entitled to notice of levy because she was not "liable" for the taxes. The Fifth Circuit Court of Appeals upheld the IRS's levy, agreeing that the wife was not entitled to notice of levy and that one-half her wages were subject to recovery. State law is used to determine a taxpayer's property interest, and once that interest is determined, federal law provides the extent to which that interest may be recovered. Under state law, the wife's income was community property, and under federal law, the IRS could recover the taxpayer's one-half interest in that property. State law protections, such as the Texas statute prohibiting one spouse's premarriage creditor from recovering from the other spouse's income, do not apply to the IRS. Although state-law protections do not apply to the IRS, the Fifth Circuit Court of Appeals concluded that creditors' rights under state law do. The court of appeals reasoned that the IRS should have no lesser rights than other creditors. Texas law provided that all the community property income of the liable spouse was subject to recovery for premarriage debts. Accordingly, the court of appeals held that the IRS could recover from *all* the husband's earnings, even though the wife owned one-half of those earnings as community property.

Section 766.55(2)(c)1. provides that after marriage, a spouse's premarriage creditor may recover only from that spouse's nonmarital property assets and from marital property assets that would have been the property of that spouse but for the marriage. Consequently, on facts similar to *Medaris* in Wisconsin concerning one spouse's premarriage tax debt, the IRS may recover from *all* earnings of the liable spouse. In addition, the taxpayer's one-half marital property interest in the nonliable spouse's earnings is also subject to recovery, notwithstanding the restrictions of section 766.55(2)(c)1., because the nonliable spouse's income is a marital (i.e., community) property asset under Wisconsin



law. State law rules for categories of obligation under section 766.55(2) are superseded by federal law and do not apply unless incorporated by federal law. *See infra* §§ 6.19, ch. 9; *see also Hollingshead v. United States*, 85-2 U.S. Tax Cas. (CCH) ¶ 9772 (N.D. Tex. 1985) (upholding seizure of taxpayer's community property interest in his wife's earnings for tax obligation for which she was not liable); Rev. Rul. 85-70, 1985-1 C.B. 361; *Calmes v. United States*, 926 F. Supp. 582 (N.D. Tex. 1996) (holding that IRS could not recover wife's earnings for husband's premarriage tax obligation because earnings were her separate property by premarital agreement); *infra* § 9.33 (effect of marital property agreements on reporting of income and property from which tax may be recovered).

The taxes due in *Vorhies v. Z. Management, Inc.*, 87-1 U.S. Tax Cas. (CCH) ¶ 9200 (W.D. Wis. 1987), arose before January 1, 1986, and were the husband's sole liability. The court permitted recovery from the husband's one-half interest in his wife's wages. The court stated that under I.R.C. § 6331, the government has authority to levy on the taxpayer's property interests and that those interests are to be determined according to state law (in this case, subsections 766.31(3) and (4)). Because the husband's tax liability was unpaid as of January 1, 1986, and because he had an interest in his wife's wages after that date, the levy was proper. Because federal law supersedes state law, section 766.55(2)(c)2. (which would have made the wife's wages unavailable for any of the husband's other pre-effective date debts) did not apply with respect to his federal taxes. Similarly, in *In re Porter*, No. C-92-4089 FMS, 1993 WL 106884 (N.D. Cal. Apr. 5, 1993), the court permitted the IRS to attach a tax lien to the husband's share of proceeds of community property real estate held by his bankruptcy trustee, even though the parties had separated (terminating the community under California law) and the state court later awarded the husband's share to the wife. At the time the real estate was sold, it was still community property, and the IRS was not bound by the award to the wife. *See also United States v. Overman*, 424 F.2d 1142 (9th Cir. 1970).

In another similar case, the U.S. District Court for the District of Arizona in *Hyde v. United States*, 93-2 U.S. Tax Cas. (CCH) ¶ 50,432 (1993), upheld the IRS's levy on the wife's community property defined-benefit plan for a postmarriage tax penalty for which only the husband was liable. This defined-benefit plan was not included in any of the exemption categories of I.R.C. § 6334(a). Initially the court upheld the levy on the husband's one-half interest in the plan based only on his state

law property interest and did not make a determination whether this debt was a separate debt or a community debt. In denying reconsideration, the court held, citing *Johnson v. Johnson*, 638 P.2d 705 (Ariz. 1981), that based on the parties' stipulation that the husband's unreported income—funds that should have been paid for taxes—had been used for community purposes, the debt was a community debt under Arizona law. Since the tax penalty was a community debt, the court stated that the wife continued to be liable, even after the death of the husband, and that her entire deferred-benefit plan was subject to levy. *Cf.* Wis. Stat. § 859.18(2), (3); *see infra* ch. 12. Although the court did not differentiate between the wife's personal liability and the availability of community property for recovery, Arizona law provides that one spouse may bind the community only for community debts, not the separate property of the other spouse, as would be the case if the other spouse were personally liable. Ariz. Rev. Stat. Ann. § 25-214(B), (C) (West, WESTLAW current through legislation effective February 9, 2010 of the Sixth Special Session, and legislation effective February 11, 2010 of the Second Regular Session of the Forty-Ninth Legislature (2010)). The distinction was immaterial to the outcome of the case because the asset against which the levy was sought was admittedly community property. *See also McIntyre v. United States*, 2 Cal. Bankr. Ct. Rep. 63 (N.D. Cal. 1998) (holding that taxpayer husband had community interest under California law in wife's share of his pension benefits, which allowed IRS to collect from her share).

In contrast to the cases involving premarriage and pre-effective date federal tax obligations, cases involving recovery from a nonliable life insurance beneficiary indicate that not all courts have allowed expansive rights of recovery by the federal taxing authorities. In *Commissioner v. Stern*, 357 U.S. 39 (1958), a state law protecting a life insurance beneficiary (the surviving spouse) from creditors' claims was held to be binding on the IRS. Under Kentucky law, absent fraud or insolvency, the beneficiary is not liable for the insured's debts. *Cf.* Wis. Stat. § 859.18(4)(a)4. (comparable Wisconsin statute). The Court found that the Internal Revenue Code (I.R.C.) section allowing the government to recover from a transferee of a taxpayer's property was only procedural and gave the government no substantive rights that would exceed any other creditor's rights under state law. *Stern*, 357 U.S. at 47; *see also O'Kane v. United States*, Civ. No. 88-1226, 1989 WL 252397 (D. Idaho Dec. 11, 1989) (holding that state law protections prevented IRS recovery from nontaxpayer spouse).

The IRS was able to recover from a life insurance beneficiary in *United States v. Bess*, 357 U.S. 51 (1958). However, unlike in *Stern*, a tax lien had been filed with respect to the taxpayer's property. See *infra* § 6.20. Since the *Bess* taxpayer before his death had had a right in the policy's cash-surrender value but not the proceeds, the government could recover from the beneficiary only to the extent of the cash-surrender value, not the proceeds. See also *LaSalle Nat'l Bank v. United States*, 636 F. Supp. 874 (N.D. Ill. 1986) (holding that state law protecting spendthrift trust is inoperative to prevent federal tax lien). The spouses' protections preventing recovery of certain property are also determined by federal law. See I.R.C. § 6334 (exemptions).

Since the IRS may exercise the rights of a creditor under state law as well as federal law, when married persons file separate returns, a question arises whether the obligation to pay income tax imposed on individual property income reported by one spouse is a family-purpose obligation under section 766.55(2)(b). It appears in most instances that federal income tax due on both marital property income and individual property income is a family-purpose obligation. But see *O'Kane v. United States*, Civ. No. 88-1226, 1989 WL 252397 (D. Idaho Dec. 11, 1989) (holding that husband's liability for failure to pay corporate tax was not community debt). A review of cases in community property states using the family-purpose doctrine indicates that an obligation incurred for the benefit of one spouse usually constitutes a family-purpose obligation. See *supra* §§ 5.9, 6.9. As such, all marital property of both spouses is available for recovery. Wis. Stat. § 766.55(2)(b); see *Hyde v. United States*, 93-2 U.S. Tax Cas. (CCH) ¶ 50,432 (holding that tax due on husband's unreported income was used for benefit of community and was community debt), *reconsideration denied*, 93-2 U.S. Tax Cas. (CCH) ¶ 50,605 (D. Ariz. 1993), *aff'd*, No. 93-16685, 1994 WL 228182 (9th Cir. 1994); see also *supra* § 6.9.

➤ **Note.** While the category of tax liability under Wisconsin law does not appear to impede the IRS's recovery of taxes, one spouse may have a remedy against the other under section 766.70(5) if the IRS recovers marital property not available to a creditor under state law because the tax debt is not a family-purpose debt. See *infra* ch. 8. Equitable factors such as whether the spouses are separated may be considered in determining whether the spouse has a right of reimbursement. Other subsections of section 766.70, such as subsection 766.70(1) relating to breaches of the duty of good faith,

may apply in certain circumstances involving the incurring and recovery of taxes. *See infra* ch. 8.

### **(3) Recovery of Wisconsin Taxes [§ 6.17]**

Unless the innocent-spouse protections apply, an income tax liability to the state of Wisconsin is treated as a family-purpose obligation under section 766.55(2)(b), and all marital property is available for recovery under section 71.91(3). No distinction is made under section 71.91(3) between tax obligations attributable to income classified as marital property and tax obligations attributable to income classified as nonmarital property reported by a spouse on a separate return. Therefore, whether an income tax liability to the state of Wisconsin on account of a spouse's individual property income reported on a separate return is family purpose or nonfamily purpose is not relevant to the taxing authorities who will be collecting the tax, but it may be of great importance to the other spouse in relation to interspousal remedies.

If the innocent-spouse rules under subsections 71.10(6)(a), (b), and (6m) apply, the tax due on a separate return may only be collected from the same property that is available for satisfying a nonfamily-purpose obligation under section 766.55(2)(d). Wis. Stat. § 71.91(3). If recovery is limited to section 766.55(2)(d), there are also limits on the rights of the Wisconsin Department of Revenue (DOR) to set off overpayments, refunds, and credits. *Id.*; *see infra* § 6.18; *see also* Wis. Stat. § 700.24 (tax liens on joint-tenancy assets). If the spouses are divorced and the divorce judgment allocates their tax liability, the judgment rather than the rules of chapter 766 apply. Wis. Stat. § 71.10(6m)(b).

#### **b. Offset of Refund, Overpayment, or Credit for Support, Taxes Due, or Debts Owed to State [§ 6.18]**

If the spouses file a joint federal income tax return for which a refund is due, and if one of them is liable for taxes due other than on the joint return, the IRS may apply the liable spouse's share of the joint refund to the amount owed. Rev. Rul. 85-70, 1985-1 C.B. 361. In the usual case in which all income is classified as marital property, the liable spouse's share will be one-half the refund because each spouse is considered to be

the recipient of one-half of all community property income and is credited with one-half of all withholding and other taxes paid. *See infra* ch. 9. Either spouse has the right to prove that some or all of the income is from noncommunity property sources of the nonliable spouse. Rev. Rul. 85-70, 1985-1 C.B. 361. On the other hand, the IRS might be able to show that state law provides that certain additional property is available for recovery; if so, the IRS may offset this amount as well. *Id.* For example, if a refund is due in a year in which all marital property income reported was earned by the spouse who is liable for taxes due for a year before marriage, all of the refund could be applied to the premarriage liability. *See* Wis. Stat. § 766.55(2)(c)1.

If a spouse who is obligated to support a former spouse or dependent children is in arrears for support, and the obligor's spouse is not liable for such support, the spouses may have their joint federal income tax refund withheld for back support under I.R.C. §§ 6305 and 6402. *See* Treas. Reg. § 301.6305-1. After notice of the intercept, the nonobligated spouse may then file a form 1040X listing the nonobligated spouse's income and claiming the portion of the refund allocable to his or her income. *See* Treas. Reg. § 301.6402-1; Rev. Rul. 80-7, 1980-1 C.B. 296. The nonobligated spouse's income would be one-half the income of both spouses that is classified as marital property, plus any income of the nonobligated spouse that is classified as individual property.

The DOR may credit an overpayment, refundable credit, or tax refund due one spouse on a separate return against amounts owed on that spouse's separate return or other amounts owed by the spouse to other state agencies and certified to the department under section 71.93. A credit or refund of one spouse may not be used to offset the liability on the other spouse's separate return. The department is required to presume that the amount of the refund or credit is classified as the nonmarital property of the filing spouse. Wis. Stat. § 71.80(3). However, if the nonfiling spouse can show by clear and convincing evidence that the state tax overpayment, refundable credit, or refund is classified as the nonmarital property of the nonfiling, nonobligated spouse, no offset will occur, and the refund or credit will be paid in full to the spouse entitled to it. *Id.*

Overpayments, refundable credits, or a tax refund due on a joint Wisconsin return may be intercepted for taxes due on joint returns or amounts certified by state agencies as due for support arrearages for dependents of one of the spouses. Wis. Stat. §§ 71.80(3m), .93. This

offset may be subject to the nonobligated spouse's claim that the overpayment, credit, or refund is classified as the nonmarital property of the nonobligated spouse. Wis. Stat. § 71.80(3m). The amount of the refund, credit, or overpayment that may be used to offset the obligated spouse's liability is limited to the proportion that the Wisconsin adjusted gross income that would have been the property of the obligated spouse but for the marriage has to the adjusted gross income of both spouses. Wis. Stat. § 71.80(3m)(b).

### **c. Other Tax Liability [§ 6.19]**

A spouse may be liable for certain other taxes unrelated to the spouses' income, such as the Wisconsin sales tax, Wis. Stat. § 77.60(2), and taxes required to be withheld from employees' income, *see* I.R.C. § 6672; Wis. Stat. § 71.83(1)(b)2.

The IRS's rights to recover taxes of any kind are discussed in section 6.16, *supra*. Wisconsin sales and use taxes may be recovered in the same manner as income taxes. Wis. Stat. § 77.62(1) (incorporating section 71.91(3), which provides that all tax obligations are incurred in interest of marriage or family); *see supra* § 6.17.

Section 71.91(3) applies to tax liability to the state only. Rules for recovery of taxes to other governmental units, such as taxes due a municipality, are determined by section 766.55(2).

### **d. Tax Liens [§ 6.20]**

If a person liable for federal tax fails to pay after demand, I.R.C. § 6321 imposes a lien "upon all property and rights to property, whether real or personal, belonging to such person." If the taxpayer's interest in his or her spouse's wages can be levied on for the taxpayer's sole tax liability, as in *McIntyre*, *Medaris*, *Vorhies*, and *Hollingshead*, *see supra* § 6.16, then it follows that a lien can attach to the taxpayer's marital property interest in an asset held by the other spouse. The statute imposes a lien on assets *belonging to* the taxpayer; it is not limited to assets *held by* the taxpayer. *See* I.R.C. § 6321; *see also United States v. Librizzi*, 108 F.3d 136 (7th Cir. 1997) (federal tax lien on one half of Wisconsin joint tenancy real estate when only one spouse is liable); *Hegg v. United States (In re Hegg)*, 239 B.R. 833 (Bankr. D. Id. 1999)

(holding that federal tax lien remained on former community property even though debtor was relieved of personal tax liability as innocent spouse).

➤ **Practice Tip.** The interests of purchasers, secured creditors, and certain other lienholders are protected from the effect of a tax lien, and those persons' rights supersede those of the government until the tax lien is properly perfected. I.R.C. § 6323(a). When a lien is perfected, however, it is not clear how these liens attach to real estate held by the nontaxpayer spouse in which the taxpayer has a marital property interest. The lien would be "hidden" because a lien search in the name of the nontaxpayer spouse would not reveal a tax lien on the taxpayer spouse's interest in the real estate held by the nontaxpayer. Under Wisconsin law, a bona fide purchaser from one spouse is protected against the assertion of the other spouse's interest, Wis. Stat. § 766.57(3), but this protection may not apply to federal taxes. Until this point is clarified, a buyer may wish to check for tax liens filed against a seller's spouse and to treat them the same as tax liens filed against the seller.

## **5. Fines, Forfeitures, and Restitution [§ 6.21]**

Under traditional community property law, one spouse is not responsible for the other spouse's criminal fines, forfeitures, or orders for restitution, and only one-half of the community property may be recovered to satisfy such obligations. William Q. de Funiak & Michael J. Vaughn, *Principles of Community Property* 432 (2d ed. 1971). The Act makes no specific provision for such obligations, but presumably they are provided for within the categories of obligations under section 766.55(2) in the same manner as other obligations. *See, e.g., Sokaogon Gaming Enter. Corp. v. Curda-Derickson (In re Marriage of Curda-Derickson v. Derickson)*, 2003 WI App 167, 266 Wis.2d 453, 668 N.W.2d 736 (holding that restitution ordered for tort of conversion could be satisfied as tort under section 766.55(2)(cm)).

## **6. Guarantees [§ 6.22]**

One type of contract obligation that can be subject to special scrutiny under the family-purpose doctrine is the guarantee or surety agreement. Such an agreement can make marital property assets subject to recovery,

even if the spouses did not receive consideration for the guarantee. An example might be the guarantee of a loan for a friend. Section 766.51, relating to management and control of marital property, does not provide specific rules for entering into guarantee agreements. Thus, a spouse having management and control of marital property may enter into a guarantee or surety agreement to the same extent that the spouse could incur any other type of credit. *Bank One, Appleton, NA v. Reynolds*, 176 Wis. 2d 218, 500 N.W.2d 337 (Ct. App. 1993); *see* Wis. Stat. § 766.51(1m). However, the issues of whether the guarantee is gratuitous and whether marital property assets are used for a purpose that is other than in the interest of the marriage or the family may arise between the spouses, in which case the nonincurring spouse may be able to bring an action to recover those assets. Wis. Stat. § 766.70(6)(a).

Since the execution of a guarantee or recovery under a guarantee signed by one spouse might result in a gift of marital property in excess of the spouse's right to make such a gift under section 766.53, Wisconsin Bankers Association forms provide for the nonincurring spouse's consent to the guarantee. This means that "both spouses act together" to make the gift of any payment or recovery under the guarantee. Wis. Stat. § 766.53. Alternatively, a signed family-purpose statement (which states that the obligation is incurred in the interest of the marriage or the family, *see supra* § 6.11) is conclusive evidence as to the creditor's right to recover marital property. *Bank One, Appleton, NA*, 176 Wis. 2d at 221. However, the statement does not affect the nonincurring spouse's right to an interspousal remedy under section 766.70. *See infra* ch. 8. Either a consent or a family-purpose statement will insulate the creditor from being treated as a gift recipient and having to disgorge the recovery. Wis. Stat. § 766.70(6)(a).

Other community property states employing the family-purpose doctrine may restrict gratuitous guarantees. For example, Arizona has a specific statute that requires joinder by both spouses on a guarantee. Ariz. Rev. Stat. Ann. § 25-214(c)(2) (West, WESTLAW current through legislation effective February 9, 2010 of the Sixth Special Session, and legislation effective February 11, 2010 of the Second Regular Session of the Forty-Ninth Legislature (2010)); *see also* Wash. Rev. Code 26.16.030(2) (West, WESTLAW current with amendments received through January 15, 2010); *Bank of Washington v. Hilltop Shakemill*, 614 P.2d 1319 (Wash. Ct. App. 1980); *Potlatch No. 1 Fed. Credit Union v. Kennedy*, 459 P.2d 32 (Wash. 1969).



The guarantee of an obligation of a member of the guarantor's immediate family probably has a family purpose under most circumstances. Similarly, there usually would be sufficient family purpose to constitute a family-purpose obligation under section 766.55(2)(b) if one spouse guarantees an obligation of a business entity in which a spouse works or owns an interest. *See, e.g., Virginia Lee Homes, Inc. v. Schneider & Felix Constr. Co.*, 395 P.2d 99 (Wash. 1964). Lenders to small businesses often require such a guarantee. A family purpose is likely to be present if the business ownership interest is classified as marital property. It may also be present if the business is classified as the guarantor spouse's individual property but generates marital property income.

If a spouse executes a guarantee agreement that results in what is arguably not a family-purpose obligation, a question arises as to when a cause of action arises under section 766.70(1) (breach of good-faith duty), section 766.70(5) (use of marital property to satisfy an obligation for other than support or family purpose), or section 766.70(6)(a) (unauthorized gift of marital property). Executing a nonfamily-purpose guarantee probably does not constitute a gift that would provide the basis for an interspousal remedy under section 766.70 and therefore does not start the various subsections' limitation periods running. There is no damage to the spouses, and no gift, until payment is made from marital property funds on account of the guarantee. Once the obligated spouse pays the nonfamily-purpose guarantee with marital property funds, a gift results and the damage to marital property is measurable, thereby giving rise to the action for the interspousal remedy.

Section 766.55(3) specifically provides that guarantee, indemnity, and surety relationships entered into before the parties' determination date for which an obligation arises after the determination date are treated as obligations in existence on the determination date. *See also* Wis. Stat. Ann. § 766.53 Legis. Council Notes—1985 Act 37, §§ 90 to 98 (West 2009). The property available for recovery by the creditor is determined under subsection 766.55(2)(c) or (d) or without reference to the Act, as the case may be, depending on whether the guarantee was executed (1) before marriage; (2) before January 1, 1986, while the parties were married; or (3) after January 1, 1986, while the parties were married but before they moved to Wisconsin. *See infra* §§ 6.23–.25, *supra* § 5.35.

## D. Predetermination Date Obligations [§ 6.23]

### 1. Obligations Incurred Before Marriage [§ 6.24]

Section 766.55(2)(c)1. states that an obligation incurred by a spouse before marriage “may be satisfied only from property of that spouse that is not marital property and from that part of marital property which would have been the property of that spouse but for the marriage.” An obligation incurred before or during the marriage that is “attributable to an obligation arising before marriage or to an act or omission occurring before marriage” may be satisfied from the same classifications of property. Wis. Stat. § 766.55(2)(c)1. Such obligations include support of dependents from a previous marriage or liability for an act, omission, or tort that occurred before marriage, if the liability is not determined until after marriage or if collection attempts are not made until after marriage. This chapter refers to these obligations as *premarriage obligations*.

Although torts are given special treatment under section 766.55(2)(cm), that section refers only to torts committed by a spouse “during marriage,” *see* Wis. Stat. § 766.01(8). Both contractual and tort obligations are included under section 766.55(2)(c)1. The following is an example of a tort obligation included under section 766.55(2)(c)1.

➤ **Example.** Assume that a single person is in an automobile accident giving rise to liability on the part of that person. He or she marries before an action is commenced, before a judgment is entered, or before full satisfaction of the judgment has been obtained. This premarriage obligation may be satisfied only from the tortfeasor’s individual property assets, predetermination date property assets, or marital property assets that would have belonged solely to the tortfeasor spouse if there had been no marriage. In the usual case, these assets include the wages of the obligated spouse but not those of the nonobligated spouse, even though each spouse has a marital property ownership interest in the other’s wages. No order of recovery is specified; therefore, the creditor need not pursue individual or predetermination date property of the obligated spouse before proceeding against the marital property. The creditor may collect from all available marital property assets, subject to allowable exemptions. Thus, the nonobligated spouse’s interest in marital

property assets generated by the obligated spouse is also subject to the obligated spouse's premarriage obligations.

Similarly, if child support or maintenance for dependents of a previous marriage comes due during a subsequent marriage, or if an obligation under a property division from a previous marriage is not satisfied before remarriage, the obligation has arisen before the subsequent marriage and will be treated as a premarriage obligation. *See* UMPA § 8 cmt.

If one spouse has a premarriage obligation that results in marital property funds being used or recovered to satisfy the obligation, the nonobligated spouse does not automatically have a right to an interspousal remedy under section 766.70(5) (recovery for marital property used to satisfy an obligation other than in the interest of the marriage or the family), nor does the obligated spouse lose his or her interest in the spouses' remaining marital property assets or any other marital property assets subsequently acquired.

➤ **Example.** If the obligated spouse's wages are garnished to satisfy his or her premarriage support obligations, the obligated spouse nevertheless continues to have a marital property interest in the nonobligated spouse's wages. This interest continues notwithstanding the fact that the nonobligated spouse lost his or her marital property interest in the obligated spouse's wages. The parties may agree to reclassify their property to reimburse the nonobligated spouse, or the nonobligated spouse may bring an action under section 766.70(5) to recover as individual property the amount of marital property so used. However, an action for reimbursement under this section is subject to equitable considerations, such as the rights of creditors who relied on the existence of the recovered property as marital property. *See also infra* ch. 8; *In re Lam*, 364 BR 379 (Bankr. N.D. Cal. 2007) (husband paid child support from prior marriage with community property when he had separate property available).

➤ **Comment.** The effect of section 766.63, relating to mixed property, on premarriage obligations of one spouse is not clear. For example, if the spouses have mixed marital property funds that would have belonged to each of them but for the marriage to such an extent that tracing these two types of marital property funds is not possible, may the premarriage creditor of one spouse recover from all such

marital property funds as if they all would have been the marital property of the incurring spouse? Since the burden of tracing is generally on the spouse wishing to preserve his or her interest in property, the burden would probably be on the nonincurring spouse to prove what marital property funds should not be available to the creditor. *See supra* § 3.20, *infra* § 6.48.

With respect to premarriage taxes incurred by a spouse, the IRS has special powers to recover marital property assets generated by both spouses. *See supra* § 6.16.

*See also* Wis. Stat. § 49.854 (liens for child support); *infra* § 6.89.

➤ **Comment.** Presumably a lien against property for delinquent support payments under section 49.854 could attach to the marital property interest of a nonliable spouse in an asset in which the liable spouse has a “recorded ownership interest.” *See* Wis. Admin. Code § DCF 152.03(7) (defining *child support lien*). The child support lien statute, however, provides a procedure for a joint owner of a levied asset to assert an interest in the property proportionate to that person’s net contribution to the property. Wis. Stat. § 49.854(7m).

## **2. Obligations Incurred While Married or Attributable to Obligation Arising While Married but Before January 1, 1986 [§ 6.25]**

The Act was not intended to change creditor-debtor relationships that arose before January 1, 1986, or to affect the pool of assets available for recovery in those relationships, even if the debtor was married when the obligation was incurred. *See* Wis. Stat. § 766.55(3); Wis. Stat. Ann. § 766.55(3) Legis. Council Notes—1985 Act 37, §§ 90 to 98 (West 2009). If a creditor-debtor relationship existed for a married person in Wisconsin when the Act became effective, January 1, 1986, but enforcement is sought after January 1, 1986, under section 766.55(2)(c)2. the creditor may recover from assets of the obligated spouse that are not marital property and from marital property assets that would have been the property of the obligated spouse but for the enactment of the Act.

➤ **Comment.** Section 766.55(2)(c)2. does not specifically apply to obligations arising while a spouse is married and literally could apply

to pre-January 1, 1986, obligations arising before marriage. However, recovery for all premarriage obligations is provided for by section 766.55(2)(c)1., leaving to section 766.55(2)(c)2. only pre-January 1, 1986, obligations incurred by a married person. The issue of which statute applies is of no consequence to the recovery because the classification of assets available for recovery is the same under either subsection of section 766.55(2)(c)—that is, the obligated spouse's nonmarital property assets and all marital property assets that would have been the property of the obligated spouse but for the marriage or but for the enactment of the Act.

Section 766.55(2)(c)2. applies to obligations enforced in Wisconsin after January 1, 1986, but incurred before that date. Because the specific date is used without reference to the spouses' determination date, the applicable obligation may have been incurred while the spouses were domiciled in another jurisdiction, as well as while they were domiciled in Wisconsin. *See also infra* § 6.30 (obligations incurred after January 1, 1986, while spouses were married and domiciled in another jurisdiction).

Torts committed by a spouse while the spouses are married but before January 1, 1986, are also subject to recovery under section 766.55(2)(c)2. Recovery for torts committed “during marriage” is provided for by section 766.55(2)(cm). *See infra* §§ 6.26–.28. The term during marriage, however, is defined by section 766.01(8) as the period during which both spouses are domiciled in Wisconsin that begins on the determination date and ends at the dissolution of the marriage or death of a spouse. Torts committed by a spouse before January 1, 1986, would have been committed before the determination date, and therefore section 766.55(2)(cm) does not apply to those torts, even though the tortfeasor was married when the tort was committed.

Section 766.70(5) provides for reimbursement to a nonobligated spouse if marital property assets are used to satisfy an obligation other than a family-purpose obligation under section 766.55(2)(b). Any obligation to which section 766.55(2)(c)2. applies, however, occurred at a time when the family-purpose doctrine was not in effect (i.e., before January 1, 1986). Whether the obligation would have been a family-purpose obligation if the Act had been in effect might be an equitable consideration in determining if the nonobligated spouse should be reimbursed under section 766.70(5).

➤ **Comment.** The result of mixing marital property available for recovery under section 766.55(2)(c)2. with marital property not available for such obligations is not clear. Since the party wishing to exclude assets from recovery usually has the burden of tracing the excludable assets, the spouse, rather than the creditor, is likely to bear that burden. *See also supra* § 6.24.

## E. Tort Obligations [§ 6.26]

### 1. In General [§ 6.27]

Section 766.55(2)(cm) governs recovery for torts committed during marriage. That section states that “[a]n obligation incurred by a spouse during marriage, resulting from a tort committed by the spouse during marriage, may be satisfied from the property of that spouse that is not marital property and from that spouse’s interest in marital property.” The creditor need not recover from nonmarital property assets before pursuing marital property assets. Section 766.55(2)(cm) was intended to protect at least part of the marital property assets from recovery for a tort obligation incurred by one of the spouses, particularly because a marital property agreement is ineffective for that purpose (except in the rare circumstance in which the creditor had notice of the agreement before the tort occurred). Wis. Stat. Ann. § 766.55(2)(cm) Legis. Council Notes—1985 Act 37, §§ 90 to 98 (West 2009); *see* Wis. Stat. § 766.55(4m). Thus, section 766.55(2)(cm) attempts to balance the property rights of an innocent spouse and the recovery rights of an injured plaintiff.

➤ **Historical Note.** The original Act contained no separate category for tort obligations. Rather, torts were originally included in the general satisfaction scheme of section 766.55(2), which required an analysis of whether the tort fell within the family-purpose doctrine. Other community property states employing the family-purpose doctrine developed the doctrine primarily in the area of tort law. Historically, the rule for recovery in those community property states that use the family-purpose doctrine was that community (family-purpose) obligations could be satisfied only from community property and separate (nonfamily-purpose) obligations could be satisfied only from separate property. *See generally* W.S. McClanahan, *Community Property Law in the United States* 488–98 (1982); *Washington*

*Deskbook*, *supra* § 6.9, at 6-35 to -52. Because of the presumption that spouses' assets are classified as community property (similar to the presumption that assets are classified as marital property under section 766.31(2)), a plaintiff in a community property state often had no property from which to recover for a separate tort. Therefore, cases interpreting the doctrine were not logically harmonious in their analyses but appeared to attempt to use the doctrine to achieve an equitable result under the circumstances.

➤ **Comment.** Section 766.55(2)(cm), added by 1985 Wisconsin Act 37 (hereinafter the 1985 Trailer Bill), generally removes the necessity of a family-purpose analysis for torts committed during the marriage. The family-purpose doctrine with respect to torts may still apply in Wisconsin, however, in the limited circumstance of determining a nonobligated spouse's right to reimbursement for marital property funds used to satisfy a nonfamily-purpose obligation. A spouse may be entitled to reimbursement if marital property funds are used or levied upon to satisfy an obligation not incurred for support or a family purpose under section 766.55(2)(a) or (b). Wis. Stat. § 766.70(5). This right of reimbursement is subject to "equitable considerations." *Id.* One of these considerations may be whether the tort would have been within the family-purpose doctrine, such as an automobile accident on the way to the grocery store, in which case reimbursement may not be equitable.

A tort creditor is limited in collection to the tortfeasor spouse's nonmarital property assets and that spouse's one-half interest in marital property assets. Wis. Stat. § 766.55(2)(cm); *see, e.g., Sokaogon Gaming Enter. Corp.*, 2003 WI App 167, 266 Wis.2d 453 (holding that restitution debt of husband for embezzlement was a tort debt). The creditor may collect the full amount of the obligation from either or both of those sources, provided that if the recovery comes solely from marital property assets, the value of the assets or the amount of the marital property funds must be large enough that one-half the value of the assets equals or exceeds the amount of the obligation. If the creditor recovers from either spouse's wages by garnishment, recovery will take longer because only one-half the wages of both spouses is owned by the tortfeasor spouse. *See infra* § 6.68 (effect of debtor's exemptions on which classification of property is available to creditors); *see also infra* § 6.37 (how marital property agreement or unilateral statement may enlarge tort creditor's rights).

The protection of the nontortfeasor spouse's interest in marital property was illustrated in *Bothe v. American Family Insurance Co.*, 159 Wis. 2d 378, 464 N.W.2d 109 (Ct. App. 1990). The defendants, husband and wife, had different automobile liability policies issued by the same carrier. Only the husband was involved in the accident that injured the plaintiff, who recovered under the husband's liability policy and then attempted to recover under the wife's policy as well. The court stated that section 766.55(2)(cm) provided that only the husband's one-half interest in marital property assets could be reached to satisfy his tort obligations—it did not subject the tortfeasor's spouse to liability for the tortfeasor's obligations. The wife's policy did not cover torts for which she was not "legally liable," and therefore the plaintiff could not recover under her policy. Similarly, the court in *K.A.G. v. Stanford*, 148 Wis. 2d 158, 434 N.W.2d 790 (Ct. App. 1988), observed that since the plaintiff in that case had not attempted to recover from the tortfeasor's spouse, the tortfeasor's spouse's insurer had no duty to defend the action on her behalf. See also *Safeco Ins. Co. v. Butler*, 823 P.2d 499, 510 (Wash. 1992) (holding that intentional act by one spouse precluded "accident" coverage of other); *Federated Am. Ins. Co. v. Strong*, 689 P.2d 68, 74 (Wash. 1984) (holding that intentional act by one spouse did not preclude collision coverage for other spouse; recovery was separate property).

The nontortfeasor spouse's interest in marital property may lose its protection under the circumstances governed by section 345.06 (owner's liability for act of operator). Section 345.06 provides:

The owners of every vehicle operating upon any highway for the conveyance of passengers for hire are jointly and severally liable to the party injured for all injuries and damage done by any person in the employment of such owners as an operator, while operating such vehicle, whether the act occasioning such injuries or damage was intentional, negligent or otherwise, in the same manner as such operator would be liable.

If such a vehicle is a marital property asset and one spouse is such an employer, it appears that this statute may make both spouses personally liable because both are "owners" of the marital property vehicle. This result would subject all of their marital and nonmarital property assets to recovery. See also Francine R. Adkins Tone, *Vehicle Owner Imputed Liability: An Exception for Community Property Owners*, 18 Lincoln L. Rev. 49 (1988) (discussing owner-liability statute in California).



## 2. Torts Committed Other Than During Marriage [§ 6.28]

Section 766.55(2)(cm) applies to torts committed “during marriage.” The Act defines the term during marriage to mean the period during which the spouses live in Wisconsin after the determination date. Wis. Stat. § 766.01(8). A tort committed by one spouse after the determination date while the spouses are married but after one of them moves from Wisconsin is not incurred during marriage. Nor is the tort obligation an “other obligation” enforceable under section 766.55(2)(d) because, like section 766.55(2)(cm), section 766.55(2)(d) applies to obligations incurred during marriage. Therefore, the Act does not apply to such an obligation, and recovery may be undertaken without reference to the Act.

Predetermination date tort obligations are treated like any other predetermination date obligations. *See supra* §§ 6.23–25. A tort committed by a spouse before marriage and for which recovery occurs after marriage is treated like any other premarriage obligation. *See supra* § 6.24. A tort committed by one spouse while the spouses are married but before January 1, 1986, is a pre-effective date obligation recoverable under section 766.55(2)(c)2. *See supra* § 6.25. Recovery for a tort committed while spouses are married and after January 1, 1986, but before both spouses reside in Wisconsin is available without reference to the Act. *See infra* § 6.30.

### F. Other Obligations [§ 6.29]

Section 766.55(2)(d) provides that “[a]ny other obligation”—that is, an obligation not covered by other categories under section 766.55(2)—that was incurred by a spouse “during marriage” may be satisfied only from the incurring spouse’s nonmarital property assets and from that spouse’s interest in marital property assets, in that order. Section 766.01(8) defines the term during marriage as the period in which both spouses are domiciled in Wisconsin that begins on the determination date and ends at the dissolution of the marriage or the death of a spouse.

Bringing an obligation within section 766.55(2)(d) generally requires overcoming the presumption in section 766.55(1) that the obligation was incurred in the interest of the marriage or the family. This may occur in

the initial proceeding or in supplementary proceedings when recovery from marital property assets is attempted. *See infra* §§ 6.51–.58. The family-purpose doctrine and the proof needed to rebut the presumption are discussed in sections 6.7–.22, *supra*. *See also* ch. 5.

The marital property assets remaining after a creditor has reached one-half of those assets continue to be classified as marital property unless and until the nonincurring spouse recovers a like amount as his or her individual property under section 766.70(5). *See infra* ch. 8; *see also* William A. Reppy, Jr., *Debt Collections from Married Californians: Problems Caused by Transmutations, Single-Spouse Management, and Invalid Marriage*, 18 San Diego L. Rev. 143, 174 (1981).

As noted above, obligations incurred by a spouse during marriage but not in the interest of the marriage or family must be satisfied first from the incurring spouse's nonmarital property assets and second from the obligated spouse's one-half interest in marital property assets, in that order. Wis. Stat. § 766.55(2)(d). No distinction is made between individual property assets and predetermination date property assets. Consequently, the creditor may elect to pursue either or both of these types of nonmarital property assets.

➤ **Comment.** Although the creditor will generally not be concerned about whether an asset is classified as the incurring spouse's individual property or predetermination property, the nonincurring spouse may prefer that the incurring spouse's individual property assets be pursued first. If the nonincurring spouse survives the incurring spouse, the nonincurring spouse may have elective rights in the deferred marital property portion of the deceased spouse's predetermination date property. The surviving spouse generally has no rights in the other spouse's individual property. A similar advantage to the nonincurring spouse may occur at divorce if nondivisible assets (such as inherited assets) rather than divisible assets (such as assets brought to the marriage by the incurring spouse) are used to satisfy the non-family-purpose obligation. However, unless payment is made voluntarily, selection of property from which recovery is made is the choice of the creditor, not the spouses.

## G. Obligations Not Provided for Under Act [§ 6.30]

The Act was not intended to change relationships between spouses and their creditors with respect to any property or obligation in existence on the spouses' determination date. Wis. Stat. § 766.55(3). Section 766.55(2)(c) leaves such relationships unaffected by providing for premarriage obligations and for pre-January 1, 1986, obligations of a spouse. Premarriage obligations may be satisfied from nonmarital property assets of the incurring spouse and from marital property assets that would have been the property of the incurring spouse but for the marriage. Wis. Stat. § 766.55(2)(c)1. Pre-January 1, 1986, obligations of a spouse (i.e., pre-effective date obligations) may be satisfied from nonmarital property assets of the incurring spouse and from marital property assets that would have been the property of the incurring spouse but for the enactment of the Act. Wis. Stat. § 766.55(2)(c)2. However, an obligation that arises while the spouses are married and after January 1, 1986, but before the spouses' determination date (i.e., while the spouses were domiciled in another jurisdiction) is not included under section 766.55(2)(c)1. or 2. Such obligations do not fit in any other category under section 766.55(2)(a)–(cm). These obligations are not satisfiable as “other obligations” under section 766.55(2)(d) because such obligations must be incurred “during marriage.” The term during marriage means the period during which both spouses reside in Wisconsin after the determination date. Wis. Stat. § 766.01(8). A post-January 1, 1986, period before spouses reside in Wisconsin would not be included. *See id.* Therefore, a creditor's recovery for such an obligation is available without reference to categories of obligations under the Act.

In addition to contract obligations, torts committed after January 1, 1986, while the spouses are married but before their determination date (i.e., while the spouses were domiciled in another jurisdiction) likewise are recoverable without reference to the Act. The general section concerning recovery for tort obligations, section 766.55(2)(cm), applies only to torts committed during marriage and thus applies only to torts committed while both spouses reside in Wisconsin after the determination date. *See* Wis. Stat. § 766.01(8); *see also supra* § 6.25 (contract and tort obligations incurred before January 1, 1986, while spouses are married).

➤ **Comment.** The Act's definition of during marriage (i.e., as the period after the spouses' determination date) appears to require the

above result with respect to torts, but it is unclear whether this result was intended.

## H. Obligations When Spouses Are Separated [§ 6.31]

Absent a marital property agreement effective as to creditors, the categories of spouses' obligations and the availability of their property to creditors are the same regardless of whether the spouses are living together or apart. A creditor may reach marital property assets held by a spouse to satisfy family-purpose obligations incurred by the other spouse, even if the nonincurring spouse received no financial benefit from or has no control over the other spouse's credit transactions. A separated spouse can protect property that he or she is earning or acquiring only by obtaining a divorce, legal separation, or future classification of property and obligations under section 766.70(4)(a)4. and 5. Creditors' rights arising after the spouses are living apart but before judgment of dissolution are not diminished by reason of their living apart. Section 766.55(2m), providing that the income of one spouse is not available to pay obligations incurred by the other, does not apply until after a decree of dissolution.

The Act has a framework of definitions that does not allow a loose interpretation of *marriage*. See also UMPA § 1 cmt. Section 766.31(4) states that income earned "during marriage" is marital property. Section 766.01(8) defines the term during marriage as the period during which both spouses are domiciled in Wisconsin that begins at the determination date and ends either at marital dissolution or at the death of a spouse. *Dissolution* in turn is defined in section 766.01(7) as termination of the marriage by entry of a decree of divorce, legal separation, annulment, or declaration of invalidity. Also, the definition of *individual property* in subsections 766.31(6) and (7) does not specifically include property acquired while living apart, and such property continues to fall automatically into the classification of marital property. See Wis. Stat. § 766.31(1). Thus, marital property assets held by either spouse while living apart remain available to creditors, as do any other marital property assets, notwithstanding the separation. This rule may produce a harsh result in some cases.

Two community property states—Washington and California—have addressed the problem of debt satisfaction and separated spouses. In Washington, for example, although section 26.16.030 of the Washington

Revised Code (West, WESTLAW current with amendments received through Jan. 15, 2010) defines *community property* as property acquired by one or both of the spouses during the marriage, case law holds that spouses may by their actions dissolve the community even though the marriage has not legally ended by a judgment of divorce. If the marriage is “defunct,” obligations and property are reclassified when the parties separate and hold themselves out as unmarried and without intention to return to the marriage. *Togliatti v. Robertson*, 190 P.2d 575 (Wash. 1948), held that the law recognizes when the marriage has in fact ended, although the facts in that particular case were so egregious that the result probably would have been found in another jurisdiction under the principle of estoppel. (The ex-wife tried to claim property in her deceased ex-husband’s estate 16 years after the divorce.) The uncertainty that may result from changes in the classifications of property and obligations without the happening of a clear event has been criticized in Carol S. Bruch, *The Legal Import of Informal Marital Separations: A Survey of California Law and a Call for Change*, 65 Cal. L. Rev. 1015 (1977).

Whether the marriage is defunct under Washington law is a question of intent. For example, a long separation resulting from one spouse’s hospitalization has been held in one case not to be evidence of abandonment of the marriage. *Rustad v. Rustad*, 377 P.2d 414 (Wash. 1963). In another case, a separated spouse who authorized her estranged husband to operate a community property business was estopped from avoiding recovery of community property assets for business debts, even though the husband was living with another woman. *Dizard & Getty v. Damson*, 387 P.2d 964 (Wash. 1964).

In assigning liability for debts in a divorce judgment, California has attempted to add certainty to the treatment of debts after separation by statutorily allocating debts for necessities to the spouses equally (this is in accord with the equal division of community property) and by allocating debts for nonnecessaries to the party who incurred the debt. If community debts exceed community property, the excess debts are allocated equitably, taking into account such factors as the parties’ relative ability to pay. See Cal. Fam. Code Ann. §§ 2551, 2620–2628 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009–2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 12 of the 2010 Reg. Sess.; and all propositions on the 6/8/2010 ballot).

### **III. Acts That Enlarge or Reduce Recovery from Marital Property [§ 6.32]**

#### **A. In General [§ 6.33]**

Sections 6.2–.31, *supra*, set forth how the various sorts of obligations incurred by a spouse are categorized and how the categories determine the property available for recovery by a creditor. Sections 6.34–.48, *infra*, deal with ways debtors and creditors may either enlarge or reduce the property otherwise available for recovery under section 766.55(2). These include security agreements, marital property agreements, consents, notices, court decrees, gifts, changes in marital status (including a change of domicile, the dissolution of the marriage, and the death of a spouse), and mixing. Certain acts may also affect the recovery by creditors of obligations in existence before the effective date of the Act, notwithstanding that section 766.55(3) provides that such relationships are not altered by the Act.

#### **B. Extension of Credit [§ 6.34]**

##### **1. Unsecured Credit [§ 6.35]**

Section 766.51(1m)(a) provides that each spouse may manage and control all assets classified as marital property (with the exception discussed below of certain marital property assets used in certain businesses) for the purpose of obtaining an extension of credit for a family-purpose obligation under section 766.55(2)(b). Section 766.56 requires a creditor to consider all marital property assets in evaluating the creditworthiness of a spouse who applies for credit that will result in a family-purpose obligation. The objective of sections 766.51(1m) and 766.56 is to promote equal access to credit by the spouse who earns less or who has fewer assets titled in his or her name.

The right to manage and control marital property for the purpose of obtaining an extension of credit is not unlimited. Unless a spouse may otherwise manage and control a marital property asset used in certain businesses described in section 766.70(3)(a)–(d), such assets may not be used by a spouse to obtain an extension of credit—that is, the creditor need not consider these assets.

## 2. Secured Credit [§ 6.36]

Management and control of an asset includes the right to create a security interest in the asset. Wis. Stat. § 766.01(11). However, a spouse may not assign, create a security interest in, mortgage, or otherwise encumber a marital property asset unless the asset is otherwise under that spouse's management and control. Wis. Stat. § 766.51(1m)(b). Under these provisions, a spouse may only encumber marital property assets that (1) are held in that spouse's name, (2) are untitled and in that spouse's possession, or (3) are held by the spouses in the alternative. A spouse may not create a security interest in marital property subject to the other spouse's exclusive management and control. *Id.* Either spouse may create a purchase money security interest in a marital property asset, however, because the spouse making the purchase has the right to hold the previously untitled property. *See also* Wis. Stat. § 766.51(1)(am), (b).

For secured transactions governed by the Uniform Commercial Code, a spouse acting alone who may manage and control marital property may sign a security agreement. Wis. Stat. § 409.203(2). (See also the detailed discussion concerning creation of security interest in marital property in chapter 5.) The managing spouse's signature is sufficient to constitute a signature of the "debtor." *See* Wis. Stat. § 409.203(4)(b). It is not necessary that both "owners" or "debtors" sign. If either section 766.55(4m) or section 766.56(2)(c) applies (relating to the creditor's actual knowledge of—or providing the creditor with a copy of—a marital property agreement or court decree under section 766.70), then the provisions of the agreement or decree apply to the creation of the security interest.

The ability to manage and control property to create a security interest is not limited to creating the interest to secure obligations within the family-purpose doctrine. The creditor having an interest in collateral is protected by section 766.55(6), which states, among other things, that the category of obligation under section 766.55(2) does not affect the right of the secured creditor to satisfaction of the obligation from the collateral. However, the use of marital property assets to secure an obligation that is not in the interest of the marriage or the family may subject the spouse who granted the security interest to an interspousal remedy under section 766.70(1) or (5).

A spouse having management and control of a marital property asset may create a security interest in the asset for an antecedent obligation as well as for an obligation incurred contemporaneously with the creation of the interest. For example, the creditor to whom a spouse owes a premarriage obligation may require that the spouse execute a security interest in marital property under the management and control of the obligated spouse, a security interest in property that would not otherwise have been available for recovery by the creditor. *See supra* § 6.24. This requirement may be in exchange for an agreement to forbear attempts at collection. The creditor's rights in the secured marital property asset are protected by section 766.55(6), but the other spouse may have a remedy against the spouse who created the interest. *See* Wis. Stat. § 766.70(1), (5).

➤ **Comment.** Many security agreements in use before the enactment of the Act, including those granting an interest in after-acquired property, refer to property “owned” by the borrower. As payments are made with marital property funds, the other spouse acquires a marital property interest in the assets pledged as collateral. *See* Wis. Stat. § 766.63(1). It is not clear whether section 766.55(6) protects the creditor's interest in collateral owned by the nonincurring spouse on account of such payments. It is similarly unclear whether section 766.55(3), which maintains creditor-debtor relationships in effect before the application of the Act, protects the creditor's interest in such collateral. While the language of the agreement is crucial, it is consistent with the policy of the Act under section 766.55(3) to interpret a provision relating to after-acquired property “owned” by the debtor to continue the security interest in after-acquired marital property assets, particularly because the managing spouse could create a new security interest in the same marital property asset. *See* Wis. Stat. § 766.51(1)(am).

A spouse's marital property interest in a life insurance policy does not affect a creditor's interest in the policy or proceeds assigned to the creditor either as security for a debt or payable to the creditor. Wis. Stat. § 766.61(4).

*See also* Wis. Stat. § 706.02(1)(f) (describing requisites for creation of security interest in homestead); *Liebzeit v. Universal Mortgage Corp. (In re Larson)*, 346 B.R. 486, 489 (Bankr. E.D. Wis. 2006) (concluding that mortgage not signed by both spouses violated section 706.02(1)(f)).



and was not valid); *Stanfield v. First Midwest Bank (In re Stanfield)*, 408 B.R. 229 (Bankr. E.D. Wis. 2009) (same); *infra* § 6.88.

### **C. Marital Property Agreement; Unilateral Statement** **[§ 6.37]**

Another method of restricting or expanding the pool of property that creditors may reach to satisfy obligations is for the spouses to enter into a marital property agreement under the Act. Marriage agreements not governed by the Act that are preserved under section 766.58(12)(a) may also affect the rights of creditors. *See infra* § 6.82 (marriage agreements in bankruptcy context). A unilateral statement under section 766.59, which makes the income on nonmarital property the individual property of the owner, is treated as a marital property agreement as it relates to the rights of third parties. Wis. Stat. § 766.59(5).

Section 766.56(2)(c) states that a creditor is not bound by a property classification, characterization of an obligation, or limitation of management and control rights in a marital property agreement or unilateral statement (or a court decree under section 766.70, *see infra* § 6.42) that affects the creditor's rights unless the agreement or statement is disclosed and the creditor is provided with a copy before credit is granted or before an open-end plan (defined in section 766.555(1)(a)) is entered into. Section 766.56(2)(c) applies to all creditors and is not limited to those who regularly extend credit. *See* Wis. Stat. § 766.01(2r)(a), (c); *Schultz v. Sykes*, 2001 WI App 260, 248 Wis. 2d 791, 638 N.W.2d 76. Knowledge or disclosure of the agreement or decree that is obtained or takes place after credit is extended does not bind the creditor with respect to the obligation or to any renewal, extension, or use of the open-end plan. Wis. Stat. § 766.56(2)(c); *see also Bank One, Appleton, NA v. Reynolds*, 176 Wis. 2d 218, 221–22, 500 N.W.2d 337 (Ct. App. 1993).

➤ **Comment.** It is not clear if it is necessary under section 766.56(2)(c) to provide a creditor with a copy of the entire marital property agreement, or if a memorandum of the agreement quoting only parts relevant to creditors' rights suffices. However, spouses may enter into more than one marital property agreement, and providing a copy of only the relevant agreement or provision is probably sufficient. If another provision of the agreement might be

relevant but is not disclosed and the creditor is not given a copy, the creditor would not be bound by the undisclosed provision.

A creditor who before the obligation is incurred has actual knowledge of a provision in a marital property agreement or unilateral statement that adversely affects the creditor's right to recover is bound by its terms, notwithstanding the fact that the creditor was not provided a copy. Wis. Stat. § 766.55(4m). Apparently the creditor's actual knowledge can be derived from either an oral or a written source, although an oral source may present problems of proof for the spouse wishing to enforce the agreement to protect property recoverable by the creditor in the absence of the agreement. The provision concerning actual knowledge applies to all creditors and not only to those who regularly extend credit. *See* Wis. Stat. § 766.01(2r)(c) (excludes section 766.55(4m) from the general definition of *creditor* in section 766.01(2r)(a) as "a person that regularly extends credit").

➤ **Note.** A marital property agreement can in some cases enlarge a creditor's recovery rights. The effect of sections 766.55(4m) and 766.56(2)(c) is to provide that a creditor without knowledge or without a copy of the agreement cannot be *adversely* affected by a marital property agreement. The benefit of the agreement is not prohibited, and creditors may take advantage of their enhanced right of recovery. For example, an "opt-in" agreement that classifies all property of the parties as marital property subjects the former nonmarital property assets of one spouse to family-purpose obligations incurred by the other spouse. *See infra* ch. 7. Also, an agreement that former marital property assets are the individual property of one spouse increases the assets recoverable by a tort creditor of the spouse owning the individual property. *See supra* §§ 6.26–.28.

Any creditor governed by the Wisconsin Consumer Act, Wis. Stat. chs. 421–427, must give notice on each loan application that the creditor is not bound by the terms of a marital property agreement or unilateral statement under section 766.59 (or a court decree under section 766.70, *see infra* § 6.42) unless the creditor is furnished a copy or has actual knowledge of the adverse provision. Wis. Stat. § 766.56(2)(b). Failure to provide the notice, unless otherwise excused, may result in liability of \$25 per applicant. Wis. Stat. § 766.56(4)(b); *Park Bank-West v. Mueller*, 151 Wis. 2d 476, 484, 444 N.W.2d 754 (Ct. App. 1989); *see infra* §§ 6.39–.41.

If a marital property agreement is entered into after an obligation is incurred, the existing creditor will not have had a copy or actual knowledge of the agreement when the obligation arose and will therefore be unaffected by the agreement. *See* Wis. Stat. §§ 766.56(2)(c), .55(4m). Any reclassification of property or limitation of management and control under the agreement will not diminish creditors' rights that arose before the agreement was executed.

➤ **Note.** If the creditor has no knowledge of a marital property agreement that *enhances* the right of the creditor to recover property, such as an agreement that reclassifies individual property as marital property, the creditor may nevertheless recover the assets that would not have been available absent the agreement.

➤ **Practice Tip.** Because marital property agreements may be ineffective with respect to creditors in those instances outlined above, parties to such agreements may wish to retain separate records relating to assets classified as individual property notwithstanding the agreement (e.g., an inheritance), as well as records relating to assets classified as individual property because of the agreement (e.g., wages). For example, assume that a spouse places funds owned at the time of the marriage in the same brokerage account into which deposits from his or her wages are also made, and that a marital property agreement classifies the wages as individual property. If the funds owned at the time of the marriage cannot be traced, they may be reached by the other spouse's family-purpose creditors who had no knowledge or copy of the agreement.

Although marital property agreements may be recorded with registers of deeds, recording does not constitute notice to third parties. *See* Wis. Stat. § 766.56(2)(a). The recording statute, section 59.43(1)(r), does not provide any restriction, requirement, or guidance as to the county in which agreements should be recorded. On the other hand, recording may be useful as evidence of the date on which the agreement was entered into and the status of particular items of property. Also, a marital property agreement containing the legal description of real estate and recorded in the county where the real estate is located does provide notice to subsequent purchasers since it appears in the chain of title under chapter 706.

A tort creditor will rarely have notice of an agreement, because of the unplanned and unintentional nature of most torts. Therefore, the property available to satisfy a tort obligation is not adversely affected by the terms of a marital property agreement. An agreement cannot be used to reduce property available for recovery for a tort unless the injured party had knowledge of the agreement before the tort occurred. *See Schultz v. Sykes*, 2001 WI App 260, 248 Wis. 2d 791, 638 N.W.2d 76.

#### **D. Creditor's Written Consent [§ 6.38]**

Another method by which collection rights can be reduced is for a creditor to consent to limited rights. Wis. Stat. § 766.55(4). The consent must be signed by the creditor and must be in writing. *Id.*

➤ **Practice Tip.** This device may be useful to a spouse who does not have a marital property agreement but who nevertheless wishes to protect a particular asset or his or her spouse's property, such as a business or the other spouse's wages. Oral agreements not to pursue certain property for collection appear to be unenforceable (because of the requirement that the consent be in writing) except to the extent that estoppel may apply under particular circumstances. The creditor's written-consent device appears not to be used widely in commercial transactions.

#### **E. Creditor's Notice to Nonapplicant Spouse [§ 6.39]**

##### **1. Wisconsin Consumer Act Transactions [§ 6.40]**

Section 766.56(3)(b) requires a creditor in a Wisconsin Consumer Act transaction to notify a nonapplicant spouse before payment is due if the other spouse has been extended credit that may result in a family-purpose obligation. The notice must describe the nature of the credit and must state that an obligation in the interest of the marriage or the family has been or may be incurred.

The statutory notice requirement is mandatory, but the Act does not specify the consequences if a creditor fails to give notice, if the applicant gives an incorrect address, or if the notice is not received. In *Park Bank-West v. Mueller*, 151 Wis. 2d 476, 444 N.W.2d 754 (Ct. App. 1989), the court of appeals found that the bank's failure to give the proper notice

under section 766.56(3)(b) to the spouse of a customer who had received a \$25,000 loan did not bar recovery of marital property assets from the nonapplicant spouse to satisfy the obligation. When the obligation was incurred, the section 766.56(3)(b) notice was addressed only to the husband, not to the nonapplicant wife or to both spouses, as is required by statute. The wife learned of the loan only after her husband's death, when the bank demanded payment. The loan balance was approximately \$15,000. *Id.* at 478.

The wife argued that the bank should not be allowed to recover from her because the section 766.56(3)(b) notice had not been given. However, the court held that the only penalty for failure to give notice is a \$25 liability, *see* Wis. Stat. § 766.56(4)(b), a penalty that the court said is so lenient as to indicate that the legislative purpose in the notice requirement was to provide information only, not to limit recovery. *Park Bank-West*, 151 Wis. 2d at 484. The court presumed this to be an unsecured consumer-credit transaction requiring section 766.56(3)(b) notice because the possibility that it was not such a transaction was not raised until appeal. *Id.* at 481–82; *see also infra* ch. 12.

## 2. Open-end Credit Plans [§ 6.41]

The Act contains special rules governing open-end credit plans that were entered into by one spouse before the spouses' determination date, but for which charges or advances under the plan were made after the spouses' determination date. *See* Wis. Stat. § 766.555. These rules apply to all such plans and are not limited to plans governed by the Wisconsin Consumer Act.

The first category of affected plans involves spouses whose determination date is January 1, 1986—that is, persons who were married and living in Wisconsin when the Act became effective. *See* Wis. Stat. § 766.555(2). The person who entered the plan could have been married or unmarried at the time of entering the plan. Creditors could give notice to the spouses of these plan participants, stating that a family-purpose obligation may be incurred under the plan and that such an obligation may be satisfied from all marital property assets, including income, as well as from the nonmarital property assets of the incurring spouse. *See* Wis. Stat. § 766.555(2)(c). The notice is considered given when mailed. It may be in an envelope addressed to the incurring spouse as long as there is notice on the outside of the envelope that it contains

important information for both spouses. *Id.* If the notice was given, then charges incurred for a family purpose under the plan after the date of the notice may be satisfied from the incurring spouse's nonmarital property assets and from all marital property. *Id.* If the notice was not given, the creditor may recover only from nonmarital property assets of the incurring spouse and from marital property assets that would have been available but for the enactment of the Act. Wis. Stat. § 766.555(2)(b).

The second category of plans affected involves spouses whose determination date is after January 1, 1986. *See* Wis. Stat. § 766.555(3). The person who entered the plan could have been unmarried or married but without an established marital domicile in Wisconsin at the time of entering the plan. In this category, obligations incurred in the interest of the marriage or the family may be satisfied from nonmarital property assets of the incurring spouse and from all marital property assets, even though no notice of the extension of credit was given to the nonincurring spouse. Wis. Stat. § 766.555(3)(c). This provision relieves the creditor of supplying notice to the nonincurring spouse, because there is no practical way for a creditor to find out that the plan participant has been married. *See* Wis. Stat. Ann. § 766.555 Legis. Council Notes—1985 Act 37, § 99 (West 2009). The provision also relieves the creditor of sending a notice when a plan participant moves to Wisconsin.

If a spouse enters into an open-end credit plan, credit advanced under the plan will usually result in a family-purpose obligation for which the creditor may recover from all marital property assets (with notice, when required, to the nonparticipating spouse that the application has been made, Wis. Stat. § 766.555(2)(c)). To avoid subjecting all marital property assets to such recovery, however, the nonparticipating spouse may, by giving notice under section 422.4155, terminate a plan governed by the Wisconsin Consumer Act. Wis. Stat. § 766.565(5). Since any plan—whether entered into before or after the spouses' determination date—may result in an obligation under section 766.55(2)(b), any right to terminate the plan would apply to all such plans at any time.

If the spouses have entered into a marital property agreement and one spouse has entered into an open-end plan, disclosure of the agreement after the plan has been entered into will not bind the creditor to collection rights set forth in the agreement upon future use of the plan. *See* Wis. Stat. § 766.55(4m). A spouse wishing to avoid recovery of marital property upon future use of a plan governed by the Wisconsin Consumer Act must terminate the plan under section 422.4155 and provide the

creditor with a copy of the marital agreement. The creditor will be bound by the agreement (or by a court decree or unilateral statement) for any new plan entered into in the future by either spouse. *See* Wis. Stat. §§ 766.55(4m), .565(5); *supra* § 6.37.

## **F. Court Orders Under Section 766.70 [§ 6.42]**

A court decree under section 766.70 may enlarge or reduce the extent of a spouse's obligations, change the classification of property, or limit creditors' collection rights in certain property. *See infra* ch. 8. Without actual knowledge of such a decree or without having received a copy of the decree before credit is extended, creditors are not bound by terms adversely affecting their rights. Wis. Stat. §§ 766.55(4m), .56(2)(c). This protection corresponds to the protection of the rights of creditors without notice of a marital property agreement. *See* Wis. Stat. §§ 766.55(4m), .56(2)(c); *see also supra* § 6.37. Creditors' rights in effect before the entry of the decree are likewise unaffected. Wis. Stat. §§ 766.55(4m), .56(2)(c).

The effect of a decree is likely to come into question when a creditor attempts to recover assets previously classified as marital property and held by the incurring spouse but reclassified in an action under section 766.70, resulting in the assets becoming the individual property of the nonincurring spouse. Without notice of the decree, the creditor may recover the reclassified assets notwithstanding the nonincurring spouse's individual property ownership of the asset.

A court order under section 766.70 may enlarge a creditor's rights, and the resulting property classification will be recognized, even if the creditor had no notice of the decree. For example, the tort creditor of a spouse who receives former marital property assets reclassified by decree as individual property may recover from all such individual property assets. The creditor is not limited to recovery from only the tortfeasor spouse's one-half interest in the assets, as it would be if the assets had remained classified as marital property. Wis. Stat. § 766.55(2)(cm).

➤ **Note.** Sections 766.55(4m) and 766.56(2)(c) refer only to court decrees under section 766.70 and not to court orders under other statutes or rules of law. Therefore, if an asset is classified by a court decree not under section 766.70 in a way that in any manner affects

the rights of a creditor without notice of the decree, the creditor is bound by the classification in the decree.

## **G. Reclassification by Gift; Gifts to Third Parties**

### **[§ 6.43]**

Gifts between spouses can reclassify property to enlarge or to reduce the pool of property available to creditors. Wis. Stat. § 766.31(10). Unless the gift is a fraudulent conveyance, *see* Wis. Stat. ch. 242 (Uniform Fraudulent Transfer Act), the creditor may not disregard the reclassification of the asset by a gift of the asset from one spouse to the other. Thus, with regard to creditors, the effect of reclassification by gift differs from that of reclassification by a marital property agreement, unilateral statement, or court decree under section 766.70, *see* Wis. Stat. §§ 766.55(4m), .56(2)(c); *see also supra* §§ 6.37, .42.

A gift of an individual property asset, or a gift of the donor spouse's marital property interest in an asset, from one spouse to the other that the donor spouse intends to be the donee's individual property reclassifies not just the asset but also the income as the donee's individual property (unless the donor provides otherwise). Wis. Stat. § 766.31(10). Such income and accumulations are therefore not available to family-purpose creditors of the donor spouse unless there has been a fraudulent conveyance.

A creditor may ask if an applicant is married, unmarried, or separated under a decree of legal separation. Wis. Stat. § 766.56(2)(d). A creditor to which the Wisconsin Consumer Act applies is also required to provide a notice that an agreement or unilateral statement under section 766.59 does not adversely affect the creditor's rights of recovery unless the creditor is provided a copy or given actual notice. Wis. Stat. §§ 766.56(2)(b), .59(5). However, asking a credit applicant about previous transfers by gift or the effect of such transfers is not specifically allowed.

A spouse having management and control of marital property may make gratuitous transfers of both spouses' interests in marital property. Wis. Stat. § 766.51(4). A gift by one spouse of marital property to a third party in excess of the limits under section 766.53 is subject to the remedies of the nonparticipating spouse; however, the right to recover such property may be exercised only by a spouse. Wis. Stat.



§ 766.70(6)(a). A creditor may not exercise a spouse's right to recover a gift of a marital property asset in excess of allowable limits. *See id.*

A gift may also occur if a spouse mixes his or her nonmarital property with marital property. Mixing reclassifies the nonmarital property as marital property unless the nonmarital property can be traced. Wis. Stat. § 766.63(1); *see supra* ch. 3; *see also infra* § 6.48 (effect on creditors' recovery).

## H. Changes in Spouse's Status [§ 6.44]

### 1. Change in Domicile [§ 6.45]

Marital property assets that are removed to another state maintain their classification and continue to be subject to recovery by creditors according to the category of obligation under section 766.55(2). *See* Wis. Stat. § 766.55(7). The assets maintain their classification even if either or both of the spouses are no longer domiciled in Wisconsin. *See* Wis. Stat. § 766.55(7); *see also* Wis. Stat. § 766.03(3). However, the classification of property acquired by spouses after either or both of them are no longer domiciled in Wisconsin is determined by the law of the new domicile.

The Act's definition of during marriage makes it clear that the term does not include any period after the effective date of the Act in which one of the spouses is not domiciled in Wisconsin. Wis. Stat. § 766.01(8). Therefore, if one of the spouses establishes a domicile outside Wisconsin, the Act no longer applies to the marriage.

➤ **Comment.** Although the cessation of the Act's applicability does not, by itself, modify rights acquired while the Act was in effect, it may have a practical effect on creditors' recovery rights that arose while the spouses were domiciled in Wisconsin. A creditor who relied on the earned income of the nonincurring spouse may have substantially diminished rights if both spouses or the spouse generating the income moves to a common law property state. *See* A.M. Swarthout, Annotation, *Change of Domicile as Affecting Character of Property Previously Acquired as Separate or Community Property*, 14 A.L.R.3d 404 (1967).

## 2. Dissolution of Marriage [§ 6.46]

The dissolution of a marriage will generally reduce the assets available to a creditor. The income of the former spouses is no longer marital property. Consequently, section 766.55(2m) provides that, unless the dissolution decree makes the nonincurring spouse responsible for the obligation, a creditor may not recover earnings of the nonincurring former spouse to satisfy a family-purpose obligation previously incurred by the other spouse.

➤ **Note.** The above provision diminishes a creditor's rights. However, the creditor's rights will not be diminished by the dissolution of the marriage if the obligation falls within the doctrine of necessities, for which both spouses are personally liable without the limitation of section 766.55(2m). *St. Mary's Hosp. Med. Ctr. v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 706 (Ct. App. 1994); *see also supra* § 6.6.

If a nonincurring spouse is assigned former marital property assets under a judgment of dissolution, that property is subject to recovery by creditors of family-purpose obligations under section 766.55(2)(b) just as it was before the judgment, but only "to the extent of the value of the [former] marital property at the date of the decree." Wis. Stat. § 766.55(2m). Any postjudgment appreciation belongs to the spouse who receives the assets. *Id.*; *see also Watters v. Doud*, 631 P.2d 369 (Wash. 1981); Annotation, *Spouse's Liability, After Divorce, for Community Debt Contracted by Other Spouse During Marriage*, 20 A.L.R.4th 211 (1983).

➤ **Comment.** Whether the creditor may recover only the asset itself or may trace the proceeds of the asset to other assets is not clear. It appears that a dollar figure would be determined to set the upper limit of the nonobligated former spouse's liability, and this amount could be recovered from the former marital property assets received in the dissolution or from any other assets traceable to the assets received. If an asset has decreased in value, it appears that the creditor may recover only the depreciated value (which is all that would have been recoverable had the marriage continued).

➤ **Note.** Section 766.55(2m) does not provide for the recovery, after dissolution, of former marital property from the nonobligated spouse

by creditors other than family-purpose creditors, and such other creditors would presumably be restricted to recovery from the spouse who is personally liable. *See, e.g., Sokaogon Gaming Enter. Corp. v. Curda-Derickson (In re Marriage of Curda-Derickson v. Derickson)*, 2003 WI App 167, 266 Wis.2d 453, 668 N.W.2d 736 (creditor intervened in dissolution action and attempted to have restitution debt of husband for embezzlement found to be a family-purpose debt; court held obligation was tort debt of husband that was not recoverable from former marital property wife received in property division).

The judgment of dissolution may provide that the nonincurring spouse is responsible for particular obligations. Such a provision would allow recovery from the nonincurring spouse's postjudgment income and from any other property as if both spouses had incurred the obligation. Wis. Stat. § 766.55(2m).

➤ **Practice Tip.** A creditor who has relied on the income of the nonincurring spouse in extending credit may wish to intervene in the dissolution action to urge that the nonincurring spouse be made responsible for the obligation after the dissolution. *See* Wis. Stat. § 803.09.

The nonincurring spouse may also be responsible for an obligation, notwithstanding whether the judgment of dissolution provides responsibility for payment, if the obligation came within the doctrine of necessities and the nonincurring spouse is found personally liable. *See supra* § 6.6. The circuit court in *St. Mary's Hospital Medical Center*, 186 Wis. 2d 100, had held that an obligation that was incurred during the marriage for medical services for the former husband, and was assigned to the husband in the dissolution decree, could be satisfied from the marital property the former wife received in the decree only to the extent of the property's value at the date of the decree. *Id.* at 110; Wis. Stat. § 766.55(2m). The court of appeals reversed the limitation and held that the obligation could be satisfied from *all* of the former wife's assets, which would include her future income. *Brody*, 186 Wis. 2d at 113. The former wife was found to be personally liable for the full amount, even though she had not incurred the debt. Since the obligation was for necessary goods and services for a spouse, it was categorized as a support obligation under section 766.55(2)(a), not a family-purpose obligation under section 766.55(2)(b) to which section 766.55(2m) applied. The court of appeals reached the same result in *Froedtert*

*Memorial Lutheran Hospital, Inc. v. Mueller*, No. 95-1449, 1996 WL 250835 (Wis. Ct. App. May 14, 1996) (unpublished opinion not citable per section 809.23(3)). *See also supra* § 6.5.

➤ **Comment.** The effect of an annulment decree on creditors' rights that arose before the decree was issued is unclear. Although the decree may declare a marriage void from its inception, the parties are considered legally married until the decree is issued. *See* Wis. Stat. § 767.313(2). A property division occurs in an annulment, just as in other dissolution actions, and thus postannulment creditors' rights could be the same as they would be after any other decree of dissolution. *See* Wis. Stat. § 767.61(1); *see also Sinai Samaritan Med. Ctr., Inc. v. McCabe*, 197 Wis. 2d 709, 541 N.W.2d 190 (Ct. App. 1995) (holding that marriage may not be annulled after spouse's death and that surviving spouse was liable for deceased spouse's medical expenses under doctrine of necessities, even though marriage appeared to be void). On the other hand, it is arguable that the nullification of the marriage results in classification of the parties' assets under common law principles, as if there had never been a marriage, and therefore no marital property assets or former marital property assets would exist.

### 3. Death of Spouse [§ 6.47]

The death of a spouse terminates the marriage, and the surviving spouse and the estate become tenants in common with respect to the former marital property. Wis. Stat. § 861.01(1). The 1985 Trailer Bill created a framework for satisfaction of spousal obligations after the death of a spouse; the framework generally follows the provisions for satisfaction of obligations during marriage. *See infra* ch. 12.

The estate may contain assets that become subject to creditors' claims, even though those assets were not available when held by the surviving spouse. For example, in *Mundell v. Mundell (In re Estate of Mundell)*, 857 P.2d 631 (Idaho 1993), the decedent's community interest in an individual retirement account (IRA) held by his surviving spouse became property of his probate estate. These funds were subject to the claims of his heirs, but they would also be subject to creditors' claims. Under Wisconsin law, an IRA would be exempt under section 815.18(3)(j) when held by a spouse, but there is no exemption from recovery by creditors for such an asset under section 859.18(4) or (5).

In addition to assets owned at the death of a spouse, the subsequent income of the surviving spouse is subject to recovery for family-purpose obligations incurred by the deceased spouse under an extension of credit (i.e., by a creditor who regularly extends credit) or for a state tax obligation. Wis. Stat. § 859.18(3). To the extent that a creditor relied for repayment on income generated by the deceased spouse, the creditor's ability to recover may be diminished (as it would have been under pre-effective date law), but the creditor's rights may be substantially protected by having available the income of the surviving spouse, even though that income is no longer marital property. This right of creditors for recovery of obligations after the death of the incurring spouse is in contrast to creditors' rights after a dissolution under section 766.55(2m). Section 766.55(2m) prohibits a creditor from recovering from the future income of the nonincurring spouse after a dissolution unless the decree provides otherwise. *See supra* § 6.46.

If the decedent spouse is the only incurring spouse for family-purpose obligations, the surviving spouse's right to receive nonprobate transfers such as life insurance, deferred employment benefits, joint tenancy property, and survivorship marital property is not subject to the claims of such creditors. Wis. Stat. § 859.18(4); *Wonka v. Cari*, 2001 WI App 274, 249 Wis. 2d 23, 637 N.W.2d 92. To the extent that such property was available to family-purpose creditors before the decedent's death, the rights of those creditors are diminished. Nevertheless, these nonprobate transfers may be subject to recovery if the obligation came within the doctrine of necessities and the surviving spouse is personally liable. *See supra* § 6.6. Assets received pursuant to a marital property agreement that provides for transfer of property at the death of a spouse are subject to recovery by creditors unless the assets were not available while both spouses were alive and the agreement is binding on the creditor. Wis. Stat. § 859.18(6).

If the surviving spouse is the only obligated or incurring spouse under section 766.55(2), those creditors may not recover certain nonprobate transfers from recipients other than the surviving spouse. Wis. Stat. § 859.18(4)(b). However, because the surviving spouse is personally liable to those creditors, other assets coming into the hands of the surviving spouse on account of nonprobate transfers upon the death of the other spouse, or on account of the surviving spouse's marital property interest in assets held by the decedent, may be available for recovery, unless the assets are otherwise exempt. *See* Wis. Stat. § 815.18(3). Assets recovered through elections may also be available. *See infra* ch.

12. Furthermore, under limited circumstances, a surviving spouse may be obliged to make elections for the benefit of certain creditors. In *Tannler v. Wisconsin Department of Health & Social Services*, 211 Wis. 2d 179, 564 N.W.2d 735 (1997), the guardian ad litem for an institutionalized surviving spouse failed to make any marital property elections after the death of the noninstitutionalized spouse. This failure to maximize resources to provide for the care of the institutionalized surviving spouse constituted divestment for Medical Assistance purposes, and the surviving spouse was denied benefits. *Id.* at 191.

## I. Mixing [§ 6.48]

Mixing nonmarital property funds with marital property funds reclassifies nonmarital property funds as marital property unless the nonmarital property funds can be traced. Wis. Stat. § 766.63(1); *see supra* ch. 3. Under this rule, a family-purpose creditor may be able to recover from funds that would not have been available had the funds not been reclassified as marital property.

➤ **Example.** A spouse with funds accumulated before marriage (individual property funds) continues to deposit earned income after marriage in the same bank account. Numerous deposits and withdrawals are made during the marriage, making it impossible to trace the individual property funds. The other spouse incurs a family-purpose obligation, and the creditor attempts to recover by garnishment of the nonincurring spouse's bank account, which now includes mixed individual property funds and marital property funds. The creditor thus is able to recover from the nonincurring spouse's individual property funds that by mixing have been reclassified as marital property.

An asset classified as nonmarital property can become classified as mixed property by a spouse's application of substantial labor resulting in substantial appreciation of the asset. Wis. Stat. § 766.63(2). Reduction of indebtedness on a nonmarital property asset using marital property funds can also result in the asset's classification as mixed property. If the nonmarital property component of the asset cannot be traced, the asset is classified as marital property. Wis. Stat. § 766.63(1). The entire asset is then subject to recovery for family-purpose obligations incurred by either spouse. *See* Wis. Stat. § 766.55(2)(b).

➤ **Comment.** The Act does not address the effects of mixing more than one type of marital property assets or funds. The effects of such mixing might be important if either spouse has premarriage or pre-effective date creditors. Obligations incurred before the marriage may be satisfied from marital property that would have been the property of the incurring spouse but for the marriage, and obligations incurred before January 1, 1986, may be satisfied from marital property that would have been the property of the incurring spouse but for the Act. Wis. Stat. § 766.55(2)(c)1., 2. Conversely, marital property generated by the nonincurring spouse is not available for recovery by the incurring spouse's premarriage or pre-effective date creditors. However, if the nonincurring spouse permits such marital property funds to be mixed with marital property funds generated by the incurring spouse (e.g., in a joint bank account), it appears, by analogy to rules relating to mixing marital and nonmarital property assets or funds, that the creditor could recover from all such funds.

## IV. Creditors' Remedies [§ 6.49]

### A. In General [§ 6.50]

The Act does not change substantive and procedural rules for establishing and enforcing the personal liability of a debtor to a creditor. In certain cases, however, the Act expands the property available to a creditor to satisfy an obligation of a debtor found personally liable. Personal liability to a creditor subjects the debtor's nonexempt nonmarital property assets to recovery by the creditor. Certain of the debtor's marital property assets are also subject to recovery, depending on the category of obligation under section 766.55(2). Thus, a nonincurring spouse's interest in marital property assets may be involuntarily recovered to satisfy family-purpose obligations incurred by the other spouse without a finding of personal liability on the part of the nonincurring spouse. This result is necessary to support the expanded availability of credit to spouses, which is discussed in chapter 5, *supra*. Whether property may be recovered depends on the classification of the spouses' property under the Act and the categories of obligations described in section 766.55(2). The property available to satisfy each category is discussed in sections 6.2–.31, *supra*, and chapter 5, *supra*. Additional factors that expand or reduce the property available to a creditor are discussed in sections 6.32–.48, *supra*.

Sections 6.51–.65, *infra*, deal with procedures available to enforce a creditor's right to reach assets determined available to satisfy the applicable category of obligation. The issue of personal liability is resolved in the initial action, and if the judgment is not satisfied, assets are recoverable by execution, garnishment, appointment of a receiver, and other creditors' remedies.

## **B. Procedures for Obtaining Judgment [§ 6.51]**

### **1. Parties [§ 6.52]**

#### **a. Actions Against Spouses [§ 6.53]**

The general rule is that for an obligation described in section 766.55(2) (which includes almost all obligations for which a spouse may be liable), a creditor may proceed against the obligated or incurring spouse alone or against both spouses. Wis. Stat. § 803.045(1); *Schultz v. Sykes*, 2001 WI App 260, 248 Wis. 2d 791, 638 N.W.2d 76. The nonobligated or nonincurring spouse is neither a necessary nor an indispensable party. If the creditor having an obligation to which section 766.55(2)(a) or (b) applies cannot obtain jurisdiction over the obligated spouse, the creditor may proceed against the nonobligated spouse alone. Wis. Stat. § 803.045(2).

Other community property states also provide for recovery from community property (or in some cases, impose joint and several liability) when only one spouse is a party. *See, e.g., Gagan v. Monroe*, 269 F.3d 871 (7th Cir. 2001) (holding that debt against husband in federal court in Indiana was enforceable against Arizona community property, and failure to join wife did not violate her due process rights); *French Mkt. Homestead, FSA v. Huddleston*, 579 So. 2d 1079 (La. Ct. App. 1991) (holding that wife was not entitled to service of foreclosure complaint concerning community property asset on which she had executed mortgage). In Washington, each spouse is treated as an agent for the community. The rule in Washington assumes that the spouse who has been served in the action will guard the interests of the nonparty spouse in the spouses' community property assets by giving that spouse appropriate notification or defending the action. *Komm v. Department of Soc. & Health Servs.*, 597 P.2d 1372 (Wash. Ct. App. 1979). The good-faith duty in Wisconsin under section 766.15 also supports that rationale.



The Wisconsin Rules of Civil Procedure provide that when the incurring spouse is a defendant, the nonincurring spouse may join or be joined as a permissive party. The nonincurring spouse is not a real party in interest in the action, but the nonincurring spouse has an interest in marital property assets that might be recovered or subject to recovery. Wis. Stat. § 803.04(3). The nonincurring spouse would not be a proper party only when that spouse has no interest in property that might be reached by the creditor, such as when the spouses have a marital property agreement classifying all their property as individual property and the creditor had a copy of the agreement before the obligation was incurred. Otherwise, marital property assets are available to satisfy all categories of obligations under section 766.55(2), although the availability of particular assets depends on which spouse generated the assets and when the obligation was incurred. For example, the nonincurring spouse's interest in marital property assets, regardless of which spouse holds the assets, is not available to satisfy a plaintiff's tort claim against the incurring spouse; only the incurring spouse's one-half interest in marital property assets held by either spouse is subject to recovery. Wis. Stat. § 766.55(2)(cm). Marital property assets remaining after the tort obligation to the plaintiff has been satisfied continue to be classified as marital property. Therefore, the incurring spouse continues to have a one-half interest in the remaining marital property assets, with the practical result of diminishing the nonincurring spouse's interest in marital property assets. *See* Wis. Stat. § 766.70(5).

In most instances of obligations other than those incurred before the spouses' determination date, it is beneficial to the creditor to join both spouses as defendants in the initial action. Doing so allows adjudication of the category of obligation at the same time that liability is determined. The judgment can (although it need not) determine the category of obligation if both spouses are joined. *See* Wis. Stat. § 806.15(4). Without a determination of category, the obligation is presumed to be within the family-purpose doctrine. *See* Wis. Stat. § 766.55(1). Joining both spouses avoids the inefficiency and expense of having that family-purpose presumption attacked by the nonjoined spouse in postjudgment proceedings in aid of execution. *See infra* §§ 6.56, .59–.62. If both spouses are joined, a determination by the court of the category of obligation is not subject to later attack. Joining both spouses also establishes and protects a judgment creditor's lien on real estate held by the nonobligated spouse. *See infra* § 6.58. If the postjudgment action is a garnishment action affecting the property of a spouse who was not a

party to the principal action, the spouse must be a defendant in the garnishment action. Wis. Stat. § 812.02(2e).

If an action in rem, such as a real estate foreclosure, relates to a marital property asset, it appears that both spouses must be joined as defendants. Wis. Stat. § 801.12(1). Section 801.12(1) states that the interests of a defendant in an asset that is the subject of an in rem or quasi in rem action may be affected only if he or she is served with a summons as provided in that section. This provision is inconsistent with section 766.01(11), which defines management and control to include both instituting and defending a civil action. If the asset that is the subject of the action is classified as marital property and is held by one spouse alone, that spouse alone should be able to defend the action. *See* Wis. Stat. § 766.51(1)(am). Therefore, because of this inconsistency, it might be the better practice to serve both spouses in a foreclosure action involving real estate that may be classified as marital property.

A practical problem arises for a creditor who wishes to join both spouses but does not know if the obligated spouse is married or does not know the name of the spouse. One possible solution is that used in *Northern Commercial Co. v. E.J. Hermann Co.*, 593 P.2d 1332 (Wash. Ct. App. 1979). The full designation of the defendants was “E.J. Hermann Co., Inc., a Washington corporation, and E.J. Hermann, and Jane Doe Hermann, his wife.” When discovery reveals the spouse’s name, the proper designation can be made, or the reference to the defendant’s spouse can be eliminated if there is no spouse. *See* Wis. Stat. § 807.12. Of course, due diligence in giving notice to the nonobligated spouse to obtain personal jurisdiction under section 801.11 would be necessary. *See Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1950).

*See also Mann v. GTCR Golder Rauner, L.L.C.*, 351 B.R. 714, 722–24 (D. Ariz. 2006) (holding that amendment of complaint to replace “Jane Doe” with defendant’s wife’s actual name related back to original complaint, making action timely as to her, when purpose of including her was to bind marital community).

If both spouses are named as defendants only because marital property may be subject to recovery, it might promote clarity to caption the action to show that only one spouse is alleged to be personally liable. For example, the caption might designate the defendants as “John Smith, individually, and John Smith and Mary Smith, husband and wife, in

relation to their marital property.” If both are alleged to be personally liable, the caption could so state. This designation was used by a trial court in *Rauen v. Kloth*, No. 87-CV-620 (Wis. Cir. Ct. Marathon County), reported in *A Pleading Suggestion*, Law. Marital Prop. F., May 1988, at 10. That case also found the nontortfeasor wife to be a proper party even though no personal liability was sought against her. The practice in some community property states is to add “as a marital community” after the names of the spouses as defendants, but Wisconsin does not recognize marital property as a separate entity, distinct from a form of ownership by the spouses.

If the spouse of a defendant is joined in the action and for any reason should not be included, the court may upon motion dismiss the spouse as a party. Wis. Stat. § 803.06(1). However, if a spouse is dismissed as a party, the spouse will not be a “named defendant in the action” and will not be “named in the judgment.” Without these designations, a judgment against the liable spouse will not result in a lien (or apparent lien) on real estate held by the defendant’s spouse. Wis. Stat. § 806.15(4); *see infra* § 6.58.

### **b. Actions by Spouses [§ 6.54]**

If a spouse is the plaintiff in an action, it appears that the plaintiff’s spouse may request to be joined as a party, or the court may join the plaintiff’s spouse as a party upon the defendant’s request, whether or not the plaintiff’s spouse is a necessary or indispensable party. Wis. Stat. § 803.04(3). This right exists even if one spouse alone has the right to bring the action. *See* Wis. Stat. § 766.51(1)(f) (providing that spouse having claim for relief under “other law” has right to manage and control action); *see also* Wis. Stat. § 766.01(11).

If the spouse of a plaintiff is joined in the action and for any reason should not be included, the court may upon motion dismiss the spouse as a party. Wis. Stat. § 803.06(1).

## **2. Pleading [§ 6.55]**

In a case in which an incurring spouse is a defendant, the complaint should contain allegations necessary to determine the spouse’s personal liability. The complaint also should contain any allegations that are

specific to the cause of action and are independent of the issue of classification of the spouse's assets or the category of the obligation under section 766.55(2), such as the statute giving rise to the action or a demand for a jury trial. The same allegations must be made if the nonincurring spouse is also included as a defendant under section 803.045(1). If the creditor wishes the right to reach all marital property assets determined in the initial action, the creditor must also allege facts sufficient to show the family-purpose nature of the obligation. *See* Wis. Stat. § 806.15(4) (judgment may determine category of obligation under section 766.55(2) if both spouses are joined). If the incurring spouse has executed a family-purpose statement under section 766.55(1), this should be stated. The creditor asserting the personal liability of a spouse under the necessities doctrine should state facts sufficient to establish liability and should include a request for such a finding in the prayer for relief.

If the plaintiff is aware, or becomes aware after discovery, that the nonobligated spouse holds marital property assets that could be subject to a judicial lien under section 806.15(4), then this allegation and a description of the property should be added to the pleadings to make the pleadings conform to the judgment identifying the property. *See infra* § 6.58.

The creditor in a Wisconsin Consumer Act transaction involving an extension of credit under section 766.56 may wish to allege that the applicant's spouse was given notice of the extension under section 766.56(3)(b), provided such a notice was actually given.

➤ **Note.** Under the holding in *Park Bank-West v. Mueller*, 151 Wis. 2d 476, 444 N.W.2d 754 (Ct. App. 1989), failure to provide notice under section 766.56(3)(b) would not affect the creditor's right to recover. The only sanction for failure to provide notice is a \$25 liability to the nonapplicant spouse. *Id.*; Wis. Stat. § 766.56(4)(b).

The creditor in a Wisconsin Consumer Act transaction may also wish to plead that it gave to the applicant proper notice under section 766.56(2)(b) (stating that no provision of a marital property agreement, unilateral statement under section 766.59, or court decree under section 766.70 adversely affects a creditor's rights unless a copy is provided) and that no such instrument was presented—again, provided such a notice was actually given.

➤ **Note.** The above allegation may not be necessary, since by analogy to *Park Bank-West*, it appears that the creditor's failure to give notice results only in the \$25 liability to the applicant imposed by section 766.56(4)(b). However, such allegations may be desirable to provide a complete picture.

If the defendant gave the creditor a copy of an agreement, a unilateral statement, or a court decree under section 766.70, or if the creditor consented in writing to limiting its rights of recovery, the defendant should plead these as affirmative defenses.

The existence, identity, and location of the defendant's spouse might not arise until discovery. *See* Wis. Stat. § 802.09 (amended pleadings).

### 3. Notice; Personal Jurisdiction [§ 6.56]

A creditor who decides to join a nonobligated spouse must serve that spouse to obtain personal jurisdiction over him or her. *See* Wis. Stat. § 801.11; *see also Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1950). The defendant obligated spouse alone has management and control of the action that can result in subjecting marital property assets to recovery by the creditor, but without joinder and proper service on the nonobligated spouse, the category of debt may be subject to collateral attack in postjudgment proceedings to enforce recovery. *See infra* §§ 6.59–.62. For example, in *Knittle v. Knittle*, 467 P.2d 200 (Wash. Ct. App. 1970), the nonincurring wife was not joined in the initial action to set arrearages for the husband's support of a child from his prior marriage. However, on appeal the court held that the wife was entitled to join in the action brought in aid of execution to collect the arrearages and to raise any defenses she could have raised in the initial action. Sections 803.03(1)(b), 806.15(4), and 812.02(2e) embody the same principle in Wisconsin.

➤ **Practice Tip.** To avoid the possibility of postjudgment litigation, it would be good practice to attempt to discover the identity and location of the defendant's spouse after the commencement of the action so the defendant's spouse could be joined under section 803.04(3) and served.

If the plaintiff with "reasonable diligence" cannot serve the defendant in an action, substituted service on the spouse of the defendant (or any

person over age 14) is the equivalent of service on the defendant and is adequate to bind the defendant personally, provided that the spouses are living together. Wis. Stat. § 801.11(1)(b). If the spouses are living apart, substituted service on the spouse under section 801.11(1)(b) is not adequate. The plaintiff can obtain personal jurisdiction by publication if with reasonable diligence the nonapplicant spouse cannot be served by personal or substituted service. Wis. Stat. § 801.11(1)(c).

#### **4. Discovery [§ 6.57]**

Permissible avenues of discovery are expanded under the Act because of the additional issues that can arise in an initial proceeding. Discoverable facts include a party's marital status, the identity of the spouse, the purpose of the transaction, and the classification of assets owned by the spouses, if such assets are subject to recovery. This information is necessary to adjudicate the category of debt under section 766.55(2).

Ordinarily the assets from which a creditor intends to recover to satisfy a judgment are not relevant in the initial action that determines personal liability. However, under the Act a judgment can include a provision that specific real property held by the spouse or former spouse of the judgment debtor is available to satisfy the obligation. Wis. Stat. § 806.15(4); *see infra* § 6.58. Information concerning any such property would therefore be subject to discovery.

#### **5. Judgment; Judgment Lien [§ 6.58]**

The findings of fact, conclusions of law, and judgment determine personal liability on the part of the obligated spouse who is the defendant in a civil action. The judgment also may determine the category of obligation and may provide that specific real estate is available to satisfy the obligation. Wis. Stat. § 806.15(4). The properly docketed judgment creates a lien on the real estate of "every person against whom the judgment is rendered" that is located in the county where the judgment is docketed. Wis. Stat. § 806.15(1). The docket includes the name and address of the judgment debtor and of the spouse or former spouse who is named in the judgment. Wis. Stat. § 806.10(1)(a). Because the latter spouse is "named" in the judgment, that spouse is included, even if he or

she was joined in an action for which he or she was not personally liable. Wis. Stat. § 806.15(4).

➤ **Comment.** It is not clear how a clerk shows on the docket that a distinction exists between a spouse who is personally liable and a spouse who is not personally liable but whose property may be affected by the judgment. However, the order for judgment might provide whether the judgment is to be docketed in the names of one or both of the spouses.

Section 806.15(4) provides that a judgment does not become a lien on real estate held by the spouse or former spouse of the judgment debtor unless (1) the spouse is named in the judgment, (2) the obligation is determined to be an obligation described in section 766.55(2), and (3) the real estate is expressly determined to be available to satisfy the obligation under section 766.55(2) or is acquired after the judgment is docketed. There is no lien if the nonincurring spouse is not a named defendant or all the other conditions under section 806.15(4) are not met. A problem arises, however, when the nonincurring spouse is a party but no specific real estate is determined to be subject to the judgment lien.

After-acquired real estate “held” by the spouse or former spouse is subject to the judgment lien if the spouse or former spouse is a named defendant. Wis. Stat. § 806.15(4)(intro.), (b). Apparently, this lien will appear on the record of real estate that is the nonmarital property real estate of the nonincurring spouse as well as on the record of marital property real estate. It appears that the lien will also appear on the record of real property held (presumably in this context, owned) by a former spouse. This may create a cloud on the title of nonmarital property real estate acquired within 10 years of a judgment by any spouse who was a named defendant. See Wis. Stat. § 806.15(1). For example, if a nonincurring spouse was joined in an action as a permissive party and is subsequently divorced, it appears that a lien attaches to all real estate acquired after the divorce, even if the real estate is marital property owned with a subsequent spouse.

Notwithstanding the apparent cloud on record title, real estate that is not available to a creditor for recovery under section 766.55(2) is exempt from execution. Wis. Stat. § 815.205(1). If execution is issued, a spouse or other party having an interest in the real estate (other than the judgment debtor who is personally liable on the judgment) may notify the officer making the levy that the real estate is exempt, and the sale

will be stayed to allow the interested party to obtain a release from the creditor. Wis. Stat. § 815.205(2). The demand for release must be made within five days of notification of the officer, and if the release is not obtained, an action for declaratory relief may be commenced under section 806.04 (the Uniform Declaratory Judgments Act) within 15 days of the demand, in which case the stay continues until the court determines the interests of the parties in the real estate. Wis. Stat. § 815.205(2)(b). Section 806.15(5) provides that such an action may be commenced 10 days after demand on the judgment creditor.

If the spouses have reclassified their assets by a marital property agreement, it may not be clear from the chain of title if real estate so classified is owned in joint tenancy, is a survivorship marital property asset, is a marital property asset, or is otherwise classified differently from the record title. Consequently, the effect of a judgment lien may not be accurately reflected in the chain of title.

The effect of a judgment lien that attaches to a spouse's interest in survivorship marital property real estate is similar to the effect of a judgment lien that attaches to a spouse's interest in real estate held in joint tenancy. While both spouses are alive, a judgment lien that attaches to only one spouse's interest in the survivorship marital property asset (i.e., only one spouse is personally liable under a family-purpose obligation) subjects the entire asset to recovery. If the judgment debtor spouse dies before execution on the judgment lien on the survivorship marital property real estate, the surviving spouse takes the decedent's interest free of the lien, unless the judgment lien is on the interests of both spouses and all the spouses' property is available under section 766.55 to satisfy the obligation—that is, both spouses are personally liable. Wis. Stat. § 766.60(5)(c). A surviving spouse receives the decedent's interest in survivorship marital property real estate, subject to tax and other statutory liens, real estate mortgages, and security interests, even though the decedent was the only incurring spouse. Wis. Stat. § 766.60(5)(b). If execution has been issued before the judgment debtor spouse dies, the surviving spouse takes the decedent's interest subject to the lien. Wis. Stat. § 766.60(5)(c).



## C. Proceedings in Aid of Execution [§ 6.59]

### 1. In General [§ 6.60]

After a creditor has obtained a judgment, whether the nonincurring spouse was joined as a defendant or was the only defendant, the creditor may proceed against either or both of the spouses to reach marital property assets subject to recovery for the judgment to the extent provided in section 766.55(2). *See* Wis. Stat. § 803.045(3). The judgment may, but need not, determine the category of obligation under section 766.55(2) and may determine that specific assets or classifications of assets are available for recovery. Wis. Stat. § 806.15(4). If the judgment is silent on those issues, the obligation is presumed to be within the family-purpose doctrine. *See* Wis. Stat. § 766.55(1). And these assets may be held by the spouse who was not the defendant in the underlying action. To enable creditors to recover marital property from both spouses for a family-purpose debt, the creditor must be able to conduct a supplementary examination of either spouse. Thus, the court of appeals in *Courtyard Condominium Ass'n v. Draper*, 2001 WI App 115, 244 Wis. 2d 153, 629 N.W.2d 38, interpreted section 816.03 to allow examination of the judgment debtor's spouse as well as the judgment debtor.

Sections 811.001 and 812.01(1) provide that attachment and garnishment actions, respectively, may affect property held by the judgment debtor or both the debtor and the debtor's spouse if an obligation under section 766.55(2) is involved. *See* Wis. Stat. Ann. § 811.001 Legis. Council Notes—1985 Act 37, § 154 (West 2007); Wis. Stat. Ann. § 812.01 Legis. Council Notes—1985 Act 37, § 156 (West 2007); *see also infra* §§ 6.62, .65. Section 816.03, relating to supplementary proceedings, was not modified by the Act. Section 816.03(1)(a) provides that the “judgment debtor” may be ordered to appear at a supplementary examination to answer questions concerning his or her property but the statute does not provide for the examination of a party who is not the “judgment debtor.” The incurring spouse may be the only defendant in the principal action, or the nonincurring spouse may be the only defendant if the creditor is unable to obtain personal jurisdiction over the obligated or incurring spouse. Wis. Stat. § 803.045(2). However, marital property assets held by either the incurring or the nonincurring spouse are available for satisfaction of family-purpose obligations.

## 2. Execution [§ 6.61]

Section 815.03 states that there are three types of executions in Wisconsin:

1. Executions against the property of the judgment debtor;
2. Executions against his or her person; and
3. Executions for delivery of property (or for damages for withholding property).

Execution may be against real or personal property. If necessary, a receiver may be appointed to collect and preserve income-producing assets subject to recovery. Wis. Stat. § 813.16. In postjudgment proceedings, as in prejudgment proceedings, it appears that notice need be given only to the spouse having management and control of an asset sought to be recovered. Wis. Stat. § 766.01(11).

➤ **Comment.** There is no provision for executing on assets held by a judgment debtor's spouse, although executing on any marital property assets necessarily includes executing on an asset in which the judgment debtor's spouse has an interest, regardless of which spouse holds title. Therefore, the phrase "property of the judgment debtor" in section 815.03 must be interpreted to mean assets available under section 766.55(2) to satisfy debts incurred by the judgment debtor, regardless of which spouse holds the property. *See also infra* § 6.62.

The issue of whether an asset is a proper subject of execution is likely to arise in a motion to quash the writ of execution brought by the nonincurring spouse who was not a party to the original action. The burden is on the objecting spouse to prove that the obligation is not a family-purpose obligation and that the plaintiff is limited to recovery of certain classifications of assets, or that the asset levied against is not marital property. *See* Wis. Stat. §§ 766.55(1), .31(2); *see also* Wis. Stat. § 903.01; *supra* § 2.25. If the asset is real estate that is not recoverable under section 766.55(2), the judgment debtor's spouse can avoid the execution and remove the lien. Wis. Stat. §§ 806.15(5), 815.205; *see supra* § 6.58.

### 3. Garnishment [§ 6.62]

Chapter 812 is divided into two subchapters, the first providing for garnishment of property other than earnings and the second providing for garnishment of earnings. A single garnishment action may recover earnings earned within pay periods beginning within 13 weeks after the date of service, and there are provisions for subsequent garnishments by other creditors for extensions beyond the 13 weeks. *See* Wis. Stat. §§ 812.35, .40. The definition of *debtor* in an earnings garnishment includes the judgment debtor's spouse whose earnings are marital property. Wis. Stat. § 812.30(4).

After obtaining a judgment against the person liable, a judgment creditor may proceed against any person who is indebted to or who has any property belonging to the creditor's debtor or property "which is subject to satisfaction of an obligation" under section 766.55(2). Wis. Stat. § 812.01(1).

A creditor holding a judgment against one spouse may proceed to recover (1) the nonmarital property of the incurring spouse and (2) marital property held by the incurring spouse, the nonincurring spouse, or both spouses, to the extent such property can be recovered for the applicable type of debt. *See* Wis. Stat. § 766.55(2); *see also* *Schultz v. Sykes*, 2001 WI App 260, 248 Wis. 2d 791, 638 N.W.2d 76. Under section 812.02(2e), a garnishment action affecting "property of a spouse" must name that spouse as a defendant. This requires naming the spouse who holds an interest in funds subject to garnishment or both spouses if both spouses have such an interest. *See* Wis. Stat. § 812.02(2e); *see also* Wis. Stat. § 705.07(1) (rights of creditors in recovering from multiple-party depository accounts). The creditor need not first obtain a judgment against the nonincurring spouse in the underlying action. Wis. Stat. §§ 812.01(1), .32. However, for the creditor to commence a garnishment action affecting the "property of a spouse" who was not a defendant in the principal action, that spouse must be made a defendant in the garnishment action. Wis. Stat. §§ 812.02(2e), .30(4); *Bank One Appleton, NA v. Reynolds*, 176 Wis. 2d 218, 222–23, 500 N.W.2d 337 (Ct. App. 1993); *see also* Wis. Stat. § 812.37(1); *Kotecki v. Marek*, No. 93-0495, 1993 WL 404321 (Wis. Ct. App. Oct. 12, 1993) (unpublished opinion not citable per section 809.23(3)).

➤ **Comment.** Interpreted literally, section 812.02(2e) requires that in all garnishments of marital property wages or other marital property assets held by either spouse, both spouses are to be named as defendants. However, such a requirement is contrary to the Act's policies regarding management and control. *See* Wis. Stat. § 766.01(11). Under the Act, management and control of marital property assets includes the right to conduct a lawsuit relating to such marital property assets held by that spouse, Wis. Stat. § 766.01(11), and it should not be necessary to name as defendant a spouse who does not hold the marital property sought to be recovered by garnishment. The Legislative Council notes on the 1985 Trailer Bill changes to section 812.01 indicate that a creditor may attempt to recover wages of a nonincurring employee spouse in a garnishment action even if judgment in the original action is against only the nonemployee spouse and the employee was not a party to the original action. Wis. Stat. Ann. § 812.01 Legis. Council Notes—1985 Act 37, § 156 (West 2007); *see also* Wis. Stat. § 812.02(2e). The notes also indicate that the nonemployee spouse need not be joined in the garnishment action because the employee spouse has management and control of his or her wages and consequently of the action.

That there may be a garnishment action to recover from the nonincurring spouse without a judgment against that spouse in the underlying action is consistent with the experience in some of the other community property states. For example, in Washington, service may be made on either spouse, and a resulting judgment based on a community obligation may be enforced against all community property even if the nonincurring spouse is not a party. *Oil Heat Co. v. Sweeney*, 613 P.2d 169 (Wash. Ct. App. 1980).

The requirement that the nonincurring spouse be joined in a garnishment action to recover from that spouse's property affords the nonincurring spouse the right to raise defenses unrelated to liability on the claim. Either the debtor or the debtor's spouse may file an answer at any time before or during the effective period of an earnings garnishment. Wis. Stat. § 812.37. When a creditor obtains a judgment against an incurring spouse without joining the nonincurring spouse, the judgment is subject to claim preclusion as to the incurring spouse's personal liability on the underlying obligation. *Schultz v. Sykes*, 2001 WI App 260, 248 Wis. 2d 791, 638 N.W.2d 76. This result is consistent with the incurring spouse's management and control of the action. *See* Wis. Stat. § 766.01(11). The defenses the nonincurring spouse might raise

include a challenge to the conclusion that the obligation was within the family-purpose doctrine or to the classification of particular assets as marital property. The nonincurring spouse thus has the right to contest the classification of particular assets that might be the individual property of the nonincurring spouse, thereby preserving due process rights.

If, however, the garnishment relates to assets under the sole management and control of the incurring spouse and the nonincurring spouse is not joined in the garnishment action, the nonincurring spouse has no opportunity to raise such issues. The incurring spouse, however, had the right to raise defenses in the underlying action and has the right in the garnishment action, a result consistent with management and control of such assets. Conduct of an action with respect to marital property is subject to the good-faith duty of the spouse having management and control. Wis. Stat. §§ 766.15(1), .70(1).

Even if both spouses are not required to be parties to a garnishment action to recover marital property funds owed to the judgment debtor, the nonincurring spouse is a permissible defendant under section 803.04(3). If the nonincurring spouse learns of the garnishment action, he or she may move to be joined. Wis. Stat. § 803.04(3). The nonincurring spouse may then raise defenses relating to the category of obligation and classification of assets available. It is doubtful that the nonincurring spouse has the right to raise other defenses relating to the litigation, as such a right would be inconsistent with the incurring spouse's management and control of the action. *See* Wis. Stat. § 766.01(11).

#### **D. Foreclosure of Mortgages; Miscellaneous Actions Involving Property [§ 6.63]**

The spouse having title to a marital property asset subject to a mortgage or security interest has management and control of that asset and thus the right to defend an action brought by the secured creditor to enforce its rights in the asset. *See* Wis. Stat. § 766.01(11); *see also supra* ch. 4. Thus, the spouse who does not hold the asset need not be joined as a party to the action to enforce the creditor's interest, even though the nontitled spouse has a marital property interest in the asset. That spouse, however, may join or be joined in the action. Wis. Stat. § 803.04(3). The creditor may wish to join the nontitled spouse if a deficiency judgment is sought, for the same reasons the creditor might wish to join the nonincurring spouse in a general civil action. *See supra* §§ 6.51–.58.

If the obligor on the note and the mortgagor are not the same (such as when one person has mortgaged real estate to secure another person's debt), each party has the right to defend the action. The purchaser of the foreclosed property takes the property free of any claim of the defendant's spouse. *See* Wis. Stat. § 766.57(3).

Actions involving homestead property have special rules and usually require joinder of the spouse on account of the resident spouse's homestead interest, even though the spouse may not have an ownership interest. *See* Wis. Stat. §§ 706.02(1)(f), 815.20.

Other actions involving both real and personal property held by one spouse alone are also subject to the management and control of only the titled spouse. *See, e.g.,* Wis. Stat. § 840.03 (actions involving interests in real property, such as partition or quiet title); Wis. Stat. ch. 810 (replevin). The creditor may sue only the spouse who has title to or possession of (if untitled) the asset regardless of its classification. *See supra* § 6.53 (parties in in rem and quasi in rem actions).

### **E. Enforcement of Security Interest [§ 6.64]**

A spouse having management and control of a marital property asset may create a valid security interest in that asset, unless the creditor is bound by a marital property agreement having provisions to the contrary. *See* Wis. Stat. § 409.203(4)(b).

The creditor seeking to recover collateral that is classified as marital property may commence an action against only the spouse who created the security interest. That spouse has management and control of the property under section 766.51(1)(am) and may defend the action. *See* Wis. Stat. § 766.01(11). Nevertheless, the other spouse having a marital property interest in the asset sought to be recovered may join or be joined in the action. Wis. Stat. § 803.04(3). Section 766.55(6) further protects a creditor's interest in collateral notwithstanding the category of the obligation, the dissolution of the marriage, or the death of a spouse, as those events do not affect the satisfaction of the obligation from the collateral. Also, regardless of the nonincurring spouse's interest in a secured property asset, the creditor holding a security interest is entitled to protection as a bona fide purchaser, provided the creditor meets all requirements for such protection. *See* Wis. Stat. § 766.57.

On the other hand, sections 801.07 and 801.12 appear to require inclusion of the nonincurring spouse in an action affecting collateral, although sections 803.04(3) and 803.045(1) make such inclusion optional. However, including both spouses as parties to an action seeking to recover a marital property asset is the only way to affect the “interests of the defendant” in an asset. Wis. Stat. § 801.07(1); *see supra* §§ 6.52–.54. In light of this apparent conflict, the creditor may wish to join the nonincurring spouse whenever possible.

## **F. Attachment [§ 6.65]**

When it appears that a defendant’s imminent conduct may affect the creditor’s ability to recover, a creditor may be entitled to attachment (seizure) of a defendant’s assets before there is sufficient time for the creditor to obtain a judgment. Wis. Stat. § 811.03(1). For purposes of a prejudgment attachment action, the term *defendant* is defined to include the defendant’s spouse or former spouse, provided that the action against the defendant involves an obligation for which marital property may be reached. Wis. Stat. § 811.001(1). The term *property of the defendant* is defined to include the marital property interest of a spouse or former spouse if the obligation is one for which marital property may be recovered. Wis. Stat. § 811.001(2).

Parties to the attachment motion are the same as the parties necessary for postjudgment collection proceedings. If only the incurring spouse is the defendant in the underlying action and the marital property asset sought to be attached is under the incurring spouse’s management and control, joining the nonincurring spouse is not necessary. Wis. Stat. § 766.01(11); *see also supra* § 6.62. The other spouse having a marital property interest may, nevertheless, join or be joined in the action. Wis. Stat. § 803.04(3).

➤ **Practice Tip.** The attachment chapter of the statutes, chapter 811, does not contain a counterpart to section 812.02(2e) of the garnishment chapter, which requires that if a garnishment affects property of the nonincurring spouse and he or she was not a defendant in the underlying action, the nonincurring spouse must be a party in the garnishment action. However, if the marital property asset sought to be attached is under the management and control of the nonincurring spouse, due process principles suggest that the nonincurring spouse should be served with notice. The category of

obligation and the question of whether the asset or a classification of assets is available to the creditor can then be adjudicated before judgment.

## **V. Debtors' Rights and Protections [§ 6.66]**

### **A. In General [§ 6.67]**

Sections 6.2–.31, *supra*, describe the categories of obligations under the Act and the classifications of assets available to satisfy each. Sections 6.32–.48, *supra*, cover typical events that might change the result under the statutory scheme. Sections 6.49–.65, *supra*, set forth the procedures by which a creditor can satisfy an obligation. Sections 6.68–.112, *infra*, deal with means by which debtors can protect assets from recovery. These include the use of exemptions, Wisconsin Consumer Act protections, and bankruptcy.

### **B. Exemptions [§ 6.68]**

Exemptions from execution are found in sections 815.18 (property exempt from execution generally) and 815.20 (homestead exemption). These are certain items, some of which are limited in value, that a debtor may retain for personal, household, and some business and farm use, notwithstanding liability to creditors. In addition, a debtor with an obligation under the Wisconsin Consumer Act has certain other exemptions, found at section 425.106. *See also In re Brien*, 128 B.R. 220 (Bankr. E.D. Wis. 1991) (holding that worker's compensation award is exempt under section 102.27(1)). Exemptions allow a debtor to retain property regardless of the claims of general creditors; a creditor having a security interest in otherwise exempt property is not defeated by these protections.

Under section 815.18(8), each spouse is entitled to claim exemptions. If the exemption is limited to a dollar amount, the spouses may combine their exemptions in the same asset or in different assets. Wis. Stat. § 815.18(8). They may not combine exemptions in the same income under section 815.18(3)(h). *Id.*; *Bank One, Appleton, NA v. Reynolds*, 176 Wis. 2d 218, 223, 500 N.W.2d 337 (Ct. App. 1993); *see also infra* § 6.90 (debtors' exemptions in bankruptcy).



For example, section 815.18(3)(b) allows an exemption for “[e]quipment, inventory, farm products and professional books used in the business of the debtor or the business of a dependent of the debtor” up to an aggregate value of \$15,000. *Dependent* is defined as any individual, including a spouse, who requires and is receiving substantial support from the debtor. Wis. Stat. § 815.18(2)(d). The purposes of allowing exemptions are to sustain life, to avoid the debtor’s becoming a public charge, and to preserve the debtor’s means of obtaining a livelihood. Wis. Stat. § 815.18(1). As previously noted, each spouse is entitled to exemptions, and they may combine their exemptions to protect a single asset or different assets. *See* Wis. Stat. § 815.18(8). Furthermore, because spouses are equally obligated to support each other, *dependent of the debtor* should include both spouses. *See* Wis. Stat. § 765.001(2) (intent of chapters 765–768). Thus, section 815.18(3)(b) would probably allow spouses to combine their exemptions in a business in which only one is active. In contrast, a bankruptcy court interpreting New Mexico law held that the spouse of a businessperson may not exempt the businessperson’s tools of the trade even though the tools are community property. *In re Bryan*, 126 B.R. 108 (Bankr. D.N.M. 1991). In that case, the relevant statute did not refer to an exemption for a dependent of the debtor, and only the person engaged in the business was allowed the exemption.

As mentioned above, exemptions relating to obligations incurred under the Wisconsin Consumer Act are also provided to debtors. *See* Wis. Stat. § 425.106. Although section 815.18(8) prevents the spouses from combining their exemptions on the earnings of one spouse, the corresponding provision under the Wisconsin Consumer Act, section 425.106(2), does not contain the earnings limitation. However, it appears that the exemption is applied to the wages of a “customer,” meaning “a person,” and that each exemption is applied to one person’s earnings. Wis. Stat. § 425.106(1)(a); *see* Wis. Stat. § 421.301(17) (defining *customer*). Therefore, the amount recoverable by the creditor would be the same as under pre-effective date law for both a consumer and a nonconsumer action.

➤ **Comment.** It appears that a debtor may choose to exempt property of any classification. If a spouse chooses to claim an individual property asset as exempt and the exemption results in recovery of nonexempt marital property assets by a creditor, a question arises whether the other spouse would have a remedy. No rule allows recovery by a spouse for the other spouse’s use of marital

property assets to satisfy a family-purpose obligation, although there may be a right to an interspousal remedy if the obligation is for other than a family-purpose obligation or if the choice of exemption results in a breach of the good-faith duty. *See* Wis. Stat. § 766.70(1), (5).

Section 815.20 sets forth the homestead exemption of \$75,000 for “debts of the owner,” which presumably can be interpreted as obligations for which the creditor could otherwise recover the homestead if it were not protected by the homestead exemption. The exemption applies to land owned by spouses jointly, in common, or as marital property. Wis. Stat. § 815.20(1). Each co-owner spouse is entitled to a \$75,000 exemption in the equity in the homestead.

### **C. Wisconsin Consumer Act Protections [§ 6.69]**

Although the original Marital Property Act left the Wisconsin Consumer Act largely unchanged, the 1985 Trailer Bill attempted to harmonize these two acts. *See* Wis. Stat. Ann. § 766.565 Legis. Council Notes—1985 Act 37, § 109 (West 2009). As a general rule, the Wisconsin Consumer Act restricts liability unless full disclosure is made to and consent is obtained from the person obligated. On the other hand, the Marital Property Act enlarges the situations under which property may be recovered to satisfy certain obligations incurred by a spouse with or without the other spouse’s knowledge or consent.

Section 766.56(3)(b) requires that creditors in transactions governed by the Wisconsin Consumer Act give notice to the nonincurring spouse that the other spouse has been extended credit that may result in an obligation in the interest of the marriage or the family. *See supra* §§ 6.39–41. This notice is not required if the nonapplicant spouse has actual notice or waives notice in writing. Wis. Stat. § 766.56(3)(c). Failure to give this notice does not diminish the creditor’s right to recover the debt. The only sanction is the \$25 liability imposed by section 766.56(4)(b). *Park Bank-West v. Mueller*, 151 Wis. 2d 476, 444 N.W.2d 754 (Ct. App. 1989).

A creditor is generally not required to give additional or separate Wisconsin Consumer Act notices to a nonincurring spouse, such as the notice of right to cure default under section 425.104. *See* Wis. Stat. § 766.565(2). There is an exception, however, in the case of an increase in an open-end-plan finance charge. *See* Wis. Stat. § 766.565(6); *see*

also Wis. Stat. § 422.415. If notice of an increase in the finance charge rate is not given to the nonincurring spouse, the new rate does not affect that spouse's interest in marital property assets. Wis. Stat. § 766.565(6). The notice may be sent to the last-known address of the incurring spouse and addressed to the incurring spouse as long as the outside of the envelope carries a notice that it contains important information for both spouses. *Id.* This requirement is consistent with the requirement that notice be sent to the nonincurring spouse when an open-end plan is entered into. *See* Wis. Stat. § 766.56(3)(b).

Under section 766.565(5), the spouse of a person who establishes an open-end credit plan may terminate the plan by giving notice under section 422.4155. The Federal Reserve Board has determined that the right to terminate an open-end plan does not violate the Equal Credit Opportunity Act. *See* Edward J. Heiser, Jr., & Robert J. Flemma, Jr., *Wisconsin's Marital Property Act: The Pain and Confusion of Converting to a Community Property System*, 42 Consumer Fin. L.Q. Rep. 42 (1988). Use of the plan is not affected until the plan is terminated, and property is available to satisfy charges made before the plan is terminated in accordance with section 766.55(2). If the nonapplicant spouse terminates a plan, this fact may be considered in future applications for credit with the creditor made by the applicant spouse. Wis. Stat. § 766.565(5).

For a discussion of the notices given to nonapplicant spouses and the property available to satisfy charges under so-called straddle plans (i.e., open-end credit plans established before the spouses' determination date and used after that date), *see* sections 6.39–.41, *supra*.

The Wisconsin Consumer Act provides protections to “customers,” defined under section 421.301(17), such as the right to redeem collateral under section 425.208. Section 766.565(3) makes clear that the spouse of a person who incurs an obligation under the Wisconsin Consumer Act has all rights and remedies available to the incurring spouse.

The Division of Banking is authorized to make rules relating to consumer transactions consistent with the policies of both the Marital Property Act and the Wisconsin Consumer Act. Wis. Stat. § 766.565(7); Wis. Admin. Code ch. DFI-WCA 1 (Wisconsin Consumer Act). The Legislative Council notes on the 1985 Trailer Bill changes to section 766.565 indicate that issues that develop with respect to the relationship between the Wisconsin Consumer Act and the Marital Property Act may

best be resolved by the rulemaking authority of the Division of Banking rather than by statutory amendment. *See* Wis. Stat. Ann. § 766.565 Legis. Council Notes—1985 Act 37, § 109 (West 2009).

## **D. Bankruptcy [§ 6.70]**

### **1. Bankruptcy Estate [§ 6.71]**

#### **a. In General [§ 6.72]**

Financial relief for individuals and certain recognized entities, with the exception of those engaged in certain specialized businesses, is provided by chapters 7, 11, 12, and 13 of title 11 of the United States Code, also known as the Bankruptcy Code.

➤ **Note on Terminology.** In the bankruptcy context, the term *debtor* means a person who or entity that files a voluntary petition in bankruptcy, or, in the case of an involuntary bankruptcy, the person against whom or the entity against which relief is ordered. *See* 11 U.S.C. § 101(13). *Nondebtor* in the bankruptcy context means the spouse of a debtor, even though the spouse may also be obligated to a creditor listed in the debtor's bankruptcy schedules.

In a Chapter 7 case, a debtor's nonexempt assets are liquidated to pay creditors. Exempt property is property that may be retained by a debtor to facilitate his or her "fresh start." *See infra* § 6.90. The nonexempt assets are collected, sold, and converted to cash by a trustee, and the net proceeds are distributed to creditors according to a system of priorities for certain categories of obligations. The debtor then receives a discharge of all dischargeable debts. *See infra* §§ 6.106–.111. The discharge operates as an injunction preventing recovery for dischargeable debts in existence on the filing date. Certain types of debts are nondischargeable. *See* 11 U.S.C. § 523.

A Chapter 11 reorganization case allows a debtor to retain possession of all property of the estate, except in unusual circumstances in which the court orders the appointment of a trustee. *See* 11 U.S.C. § 1104. The debtor, in this context known as the *debtor-in-possession*, has all the powers of a trustee. The Chapter 11 debtor, or sometimes other interested parties, may propose a plan for reorganization or orderly

liquidation of the debtor's assets and a schedule of distributions to creditors. The plan must be proposed in good faith, and creditors must receive at least as much as they would have received under a Chapter 7 liquidation. 11 U.S.C. § 1129. Creditors vote on the plan, and the court confirms the plan if all statutory requirements are met. *Id.* Upon confirmation of the plan, the debtor obtains a discharge of all dischargeable debts except to the extent they are provided for in the plan. 11 U.S.C. § 1141(d).

A Chapter 12 case may be filed only by individuals and farming or fishing operations with regular income that meet the definition of *family farmer or family fisherman* and other related definitions in 11 U.S.C. § 101. 11 U.S.C. § 109(f). The debtor remains in possession although the debtor-in-possession may be removed under certain circumstances. *See* 11 U.S.C. § 1204. Requirements for confirmation of a plan and plan administration are similar to those in a Chapter 13 case.

A Chapter 13 case enables a debtor to propose a plan of repayment of some or all debts over three (or sometimes up to five) years. 11 U.S.C. § 1322(d). To qualify for filing a Chapter 13 case, an individual (or an individual and the individual's spouse) must have a regular income and not more than \$1,081,400 in secured debts and \$360,475 in unsecured debts. 11 U.S.C. § 109(e). Payments are made to a Chapter 13 trustee who administers the plan and pays creditors. 11 U.S.C. § 1322(a)(1). Some debts provided for by the plan may be paid directly to the creditor by the debtor. The debtor retains possession of all exempt and nonexempt property. If the plan is proposed in good faith, pays creditors no less than they would have received under Chapter 7, and meets other requirements for confirmation, the court confirms the plan. 11 U.S.C. § 1325. On completion of the plan, the debtor receives a discharge of all unpaid dischargeable debts. 11 U.S.C. § 1328.

State property law determines ownership rights that a person or entity may have in various types of property, and these rights determine the property's treatment under the Bankruptcy Code. 5 *Collier on Bankruptcy* ¶ 541 (15th ed. 2003) [hereinafter *Collier*]. Since marital property has the essential characteristics of community property and is based on the same principles as community property, it is treated as community property under the Bankruptcy Code. *See* Wis. Stat. § 766.001(2) ("It is the intent of the legislature that marital property is a form of community property."). Therefore, the discussion of bankruptcy

in this chapter uses the terms *community property* and *marital property* interchangeably.

The bankruptcy schedules, which must be filed by every debtor, disclose the debtor's assets, creditors, income, expenses, and other pertinent information relating to the debtor's financial condition. *See* Official Bankruptcy Form 6, at <http://www.uscourts.gov/bkforms/index.html>. Individual debtors must disclose whether assets are owned by the husband, by the wife, jointly, or as community property. *See id.* The debtor must also disclose who is liable to each creditor—the husband, the wife, both spouses, or the “community.” *See id.* Although Wisconsin does not recognize a “community” or “marital” obligation, this designation is loosely analogous to a family-purpose obligation.

➤ **Note.** The Wisconsin Marital Property Act and the Bankruptcy Code differ in how particular classifications of property may be recovered for satisfaction of various types of obligations. Rules for satisfaction of creditors under section 766.55(2) do not apply in the bankruptcy context. *See infra* § 6.105. When a case is within the jurisdiction of the bankruptcy court and state and federal rules differ, the federal rules control.

On April 20, 2005, President George W. Bush signed into law the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), Pub. L. No. 109-8, 119 Stat. 23. Most provisions became effective for cases filed on or after October 17, 2005, but some changes, such as certain homestead-exemption provisions, were effective on enactment. BAPCPA constitutes a substantial and comprehensive revision of bankruptcy law, the details of which are beyond the scope of this text. For more information, see Randall D. Crocker et al., *No Small Change: The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* (State Bar of Wisconsin CLE Books 2005). However, issues involving marital property often entail other consumer and business issues as well, and attorneys are encouraged to become familiar with the changes in bankruptcy law or to consult experienced bankruptcy counsel when these issues arise.

A few of the more notable changes are as follows:

1. A *means test* was established to determine eligibility for a Chapter 7 discharge for debtors whose debts are primarily consumer debts. 11 U.S.C. § 707(b). This applies primarily to higher income debtors,

but the standard for dismissal of any Chapter 7 case was changed from *substantial abuse* to *abuse*. *Id.* The standing of creditors to bring a motion to dismiss for abuse of the Bankruptcy Code was expanded.

2. The time between eligibility for Chapter 7 discharges was extended from six years to eight. 11 U.S.C. § 727(a)(8). A time limit was also established for obtaining a Chapter 13 discharge after a discharge in another chapter has been obtained. 11 U.S.C. § 1328(f).
3. Exceptions to the automatic stay, especially for collection of payments for support of dependents, were expanded. Wage orders and tax intercepts for collection of support payments are not stayed, even if collection is from property of the estate. 11 U.S.C. § 362(b)(2).
4. Nondischargeable support obligations are now defined as *domestic support obligations*, 11 U.S.C. § 101(14A), and the categories of claimants were expanded, including the addition of support debts due to a governmental unit, 11 U.S.C. § 101(14A)(A)(ii).
5. Property division debts are now excepted from discharge. Equitable defenses were eliminated, and it is no longer necessary to file an adversary proceeding to have the debt excepted from discharge. 11 U.S.C. § 523(a)(15).
6. Domestic support obligations are elevated to first-priority claims, subject only to expenses of the trustee in recovering funds to pay such claims. *Compare* 11 U.S.C. § 507(a)(1)(A) *with* 11 U.S.C. § 507(a)(1)(C). These claims must be paid in full in a plan, unless the claimant consents to other treatment. Governmental support claims need not be paid in full, but a Chapter 13 plan with this provision must extend for five years. 11 U.S.C. § 1322(a)(4). Plans for higher income debtors under a Chapter 13 means test must extend for five years as well. 11 U.S.C. § 1325(b)(4)(A)(ii).
7. Domestic support obligations that accrue after filing must be paid to have a plan confirmed, 11 U.S.C. §§ 1225(a)(7), 1325(a)(8), and Chapter 12 and 13 debtors must certify that all such obligations are paid before a discharge is issued, 11 U.S.C. §§ 1228(a), 1328(a). Failure to make such payments is grounds for dismissal of the case.

8. Length of time of domicile in a state has been increased for the purpose of claiming exemptions. 11 U.S.C. § 522(b)(3). Also, there are limitations on the homestead exemption, and expanded recovery of fraudulent transfers, for debtors found to have committed certain wrongful acts. Provisions regarding the homestead exemption were effective on the date of enactment.
9. Debtors are subject to increased disclosure requirements at the beginning of a case and during the pendency of a plan. 11 U.S.C. § 521(e)(2)(A). Creditors can obtain copies of tax returns filed while the plan is in effect. 11 U.S.C. § 521(f).
10. Debtors are required to meet credit-counseling requirements to file a case, except in special circumstances, and to obtain a discharge. 11 U.S.C. § 109(h)(1).
11. The Chapter 13 discharge no longer encompasses debts incurred by fraud, defalcation in a fiduciary capacity, or personal injury caused by willful or malicious acts. 11 U.S.C. § 1328(a)(2).
12. Creditors holding security interests in motor vehicles and other personal property are protected from “cramdown” in a Chapter 13 plan, 11 U.S.C. § 1325(a), by lien-avoidance limitations, 11 U.S.C. § 522(f), and in reaffirmation procedures, 11 U.S.C. § 524(c). Rights of creditors holding claims for cash advances and luxury goods are expanded in exceptions to discharge under all chapters. 11 U.S.C. § 523(a)(2)(C). The value of collateral for Chapter 7 and 13 debtors is generally retail value. 11 U.S.C. § 506(a)(2).
13. Withholding by employers and payments by debtors to qualified benefit plans are not counted as property of the estate. Also, certain educational trusts set up for children during a set period before filing are excepted from property of the estate. 11 U.S.C. § 541(b).
14. The automatic stay may not be in effect for particular property if serial cases have been filed and earlier ones dismissed. 11 U.S.C. § 362.
15. There are new provisions for an individual Chapter 11 case. The individual Chapter 11 debtor’s earned income is property of the estate. 11 U.S.C. § 1115.



16. There is increased liability for attorneys filing cases for debtors, requiring reasonable investigation into information submitted by the client. There is a new definition of *debt relief agency*, requiring certain disclosure and record-keeping requirements when giving bankruptcy advice to certain persons. 11 U.S.C. §§ 526–528.

➤ **Note.** In *Milavetz, Gallop, & Milavetz, P.A. v. United States*, 130 S. Ct. 1324 (2010), the U.S. Supreme Court held that attorneys are considered to be debt relief agencies, and that debt relief agencies, including attorneys, although prohibited from advising people to incur more debt in contemplation of filing bankruptcy, are not prohibited from advising people to incur more debt for “valid purposes” or from discussing the consequences of acquiring additional debt.

### **b. Who May File Voluntary Petition [§ 6.73]**

Under Chapters 7, 9, 11, 12, and 13 of the Bankruptcy Code, only a person or entity recognized under 11 U.S.C. § 109 may file a voluntary bankruptcy petition. The prerequisites of 11 U.S.C. § 109 do not include obtaining consent from an individual’s spouse, and accordingly, one spouse alone may file. Although a married person may wish to file a bankruptcy petition only as to his or her interest in marital property assets and related obligations, thereby attempting to protect the nonmarital property assets of either or both of the spouses, the aggregate community property of a married couple is not considered an entity. Consequently, a spouse or spouses may not treat their community property as an entity for the purpose of declaring bankruptcy. *In re Wallace*, 22 F.2d 171 (E.D. Wash. 1927); *see 4 Collier, supra* § 6.72, ¶ 541.15. One spouse (or both, if they file a joint petition under 11 U.S.C. § 302) must also subject his or her separate property (in Wisconsin, individual and predetermination date property) to inclusion in the bankruptcy estate. The spouse who does not file the petition keeps his or her nonmarital property assets outside the jurisdiction of the bankruptcy court. *See also infra* § 6.91 (discussion of rules for who may be subject to involuntary petition in bankruptcy); *In re McDonald*, No. Civ. A. 93-4176, 1994 WL 160484 (E.D. La. Apr. 22, 1994) (holding that wife could not file joint petition without husband’s consent, even though community property encumbered by community claims was in her bankruptcy estate); Fed. R. Bank. P. 1004.1 (filing by power of attorney).

For federal law purposes, it appears that only a husband and wife can file a joint petition. In *In re Kandu*, 315 B.R. 123 (Bankr. W.D. Wash. 2004), the debtor and her same-sex partner had been legally married in Canada, but the court held that they had no right to file a joint case under the Bankruptcy Code because the court had no obligation to give full faith and credit to the Canadian marriage. Furthermore, even if the couple had been legally married in one of the states that allows same-sex marriages, the Defense of Marriage Act, 1 U.S.C. § 7, does not prohibit such marriages; it only determines how such marriages are treated under federal law.

It is less clear whether former spouses who are subject to a Wisconsin decree of legal separation can file a joint petition. Section 766.01(7) includes legal separation in the definition of *dissolution*. After dissolution, marital property rules no longer apply to the parties' assets. See Wis. Stat. § 766.01(8) (definition of during marriage); see also Patricia K. Ballman, *Legal Separation: Is It a Termination of Marriage or a Suspension of Marriage?*, 25 Wis. J. Fam. L.1 (2005). Nevertheless, parties to a legal separation are not free to remarry others, and they can apply for a revocation "at any time after the judgment" of separation. Wis. Stat. § 767.35(4). On stipulation of the parties within a year after the judgment, or by motion of one party after a year, the court "shall" convert the judgment of legal separation to a divorce judgment. Wis. Stat. § 767.35(5); see also *Bartz v. Bartz*, 153 Wis.2d 756, 452 N.W.2d 160 (Ct. App. 1989) (construing statute's use of "shall" as mandatory).

➤ **Comment.** *Spouse* is not a defined term under the Bankruptcy Code, and only an individual and that individual's spouse can file a joint bankruptcy petition. 11 U.S.C. § 302. No cases have decided the issue in this state, but it is probable that courts would interpret the definitions of dissolution and during marriage under the Wisconsin Marital Property Act to put legally separated spouses outside the qualification for a joint bankruptcy petition.

Section 109(e) of the Bankruptcy Code provides for who may qualify as a Chapter 13 debtor. Relief under Chapter 13 is available only to "an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than \$360,475 and noncontingent, liquidated, secured debts of less than \$1,081,400, or [with the same liability limitations] an individual with regular income and such individual's spouse." 11 U.S.C. § 109(e).

➤ **Comment.** There may be circumstances in which a person might be personally liable for unsecured debts of less than \$360,475, but because of obligations incurred by his or her spouse, there might be unsecured community claims of more than \$360,475. Since the statute designates an individual that “owes,” rather than an individual with an interest in property that could be recovered for a debt, it appears that only personal liability is used to determine a married debtor’s eligibility for relief under Chapter 13.

If only one spouse files, creditors of both spouses having community claims are entitled to notice. 11 U.S.C. § 342. Local Bankruptcy Rules for the Eastern District of Wisconsin 1005, 1007.1–.3 require disclosure of certain information concerning the debtor’s spouse to facilitate notice to interested parties. *See also In re Sweitzer*, 111 B.R. 792, 798–99 (Bankr. W.D. Wis. 1990) (discussing notice requirements in one-spouse filings in community property state).

### **c. Property of Estate [§ 6.74]**

#### **(1) Debtor’s Nonmarital Property and Marital Property Under Debtor’s Sole, Equal, or Joint Management and Control [§ 6.75]**

The filing of a bankruptcy petition creates an estate consisting of the bankruptcy debtor’s separate (nonmarital) property assets. 11 U.S.C. § 541(a)(1). The estate includes assets that were never classified as marital property, plus any assets that were formerly classified as marital property, such as assets acquired on account of the death of the debtor’s spouse before the bankruptcy petition was filed or assets awarded to the debtor in a dissolution action before the petition was filed. The estate also includes any community (marital) property assets under the debtor’s management and control. 11 U.S.C. § 541(a)(2)(A). Section 541(a)(2)(A) of the Bankruptcy Code states:

Property of the estate.

(a) The commencement of a case under section 301, 302 or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

...

(2) All interests of the debtor and the debtor’s spouse in community property as of the commencement of the case that is—

(A) under the sole, equal or joint management and control of the debtor;

...

The application of 11 U.S.C. § 541(a)(2)(A) to Wisconsin marital property results in the inclusion of all property under the debtor's management and control in the estate, including (1) all the debtor's nonmarital property assets, (2) all marital property assets titled in the debtor's name alone or titled in the debtor's and the debtor's spouse's names in the conjunctive or in the alternative, and (3) untitled assets in the debtor's possession. *See* Wis. Stat. § 766.31; *see also Ragan v. Commissioner*, 135 F.3d 329 (5th Cir. 1998); *Kapila v. Morgan (In re Morgan)*, 286 B.R. 678 (Bankr. E.D. Wis. 2002); *In re Lang*, 191 B.R. 268 (Bankr. D. P.R. 1995).

As a general rule, marital property assets held by one spouse are not subject to the other spouse's management and control. Wis. Stat. § 766.51(1). Nevertheless, section 766.51(1m) provides that each spouse acting alone may manage all marital property assets for the purpose of obtaining an extension of credit for a family-purpose obligation. There are exceptions for certain business-related marital property assets or business interests classified as marital property and described in section 766.70(3)(a)–(d), which are not subject for any purpose to the management and control of the spouse not holding the property. Arguably, the nonholding spouse's management and control of nonbusiness-related marital property assets for the limited purpose of obtaining an extension of credit brings those assets into the bankruptcy estate of the nonholding spouse under 11 U.S.C. § 541(a)(2)(A). However, since such control is limited and indirect, a more logical interpretation is that once the pre-bankruptcy debt is incurred, the debtor's management and control rights cease. Under this second view, the nondebtor's marital property non-business-related assets are not part of the debtor's bankruptcy estate under 11 U.S.C. § 541(a)(2)(A), although they may be included under 11 U.S.C. § 541(a)(2)(B). *See infra* § 6.76.

**(2) Marital Property Assets Liable for  
Allowable Claim Against Debtor or  
Against Both Debtor and Debtor's Spouse  
[§ 6.76]**

In addition to marital property assets under the debtor's sole, equal, or joint management and control under 11 U.S.C. § 541(a)(2)(A), which are fully included in the estate, *see supra* § 6.75, all other assets classified as marital property held by the nondebtor spouse are included in the estate "to the extent" those assets are "liable for an allowable claim" against the debtor or against both the debtor and his or her spouse. 11 U.S.C. § 541(a)(2)(B). Because all marital property held by either spouse may be recovered for a family-purpose debt, Wis. Stat. § 766.55(2)(b), all marital property assets other than those included in the estate under 11 U.S.C. § 541(a)(2)(A), including marital property business-related assets and business interests, are subject to inclusion in the estate under 11 U.S.C. § 541(a)(2)(B). *See also* Wis. Stat. § 766.70(3)(a)–(d).

➤ **Comment.** Whether nonbusiness-related marital property assets held by the nondebtor spouse are includible under 11 U.S.C. § 541(a)(2)(A) or (B) may be important in a case in which such assets are involved. The ability to exclude these assets from the debtor's estate affords protection of those assets from the debtor spouse's creditors.

It is clear from the foregoing that categories of property included in the estate under 11 U.S.C. § 541(a)(2) do not neatly correspond to the classifications of property under the Marital Property Act. To determine whether marital property assets held by the nondebtor spouse are includible under 11 U.S.C. § 541(a)(2)(B), what constitutes a "claim" under this section must be determined. A claim is basically the right of a creditor to payment. 11 U.S.C. § 101(5). Under 11 U.S.C. § 102(2), a claim against the debtor includes a claim against property of the debtor; thus, a creditor that may recover from community property in which the debtor has an interest has a claim against the debtor, even if the debtor is not personally liable to the creditor. For the purpose of including property in the estate in the first instance, without regard at this point to how it will later be distributed to creditors, reference to state law concerning obligations and the ability of creditors to reach particular assets is necessary. This rule was intended to allow creditors access to property in the bankruptcy estate that would have been available under

state law, although there may be significant differences. See Alan Pedlar, *Community Property and the Bankruptcy Reform Act of 1978*, 11 St. Mary's L.J. 349 (1979). But see *infra* § 6.105 (rights of creditors to payment from property of estate).

All property of the spouses is potentially includible in the bankruptcy estate because of the presumption in Wisconsin that all property of the spouses is classified as marital property and the rule that all marital property assets may be recovered by creditors to satisfy a family-purpose obligation. Wis. Stat. §§ 766.31(2), .55(2)(b); see *Danning v. Burg (In re Burg)*, 103 B.R. 222 (B.A.P. 9th Cir. 1989) (holding that nondebtor wife's declaration that she had received gift but could not remember into which account it was deposited was insufficient to rebut presumption that asset was community property); cf. *Schwaber v. Reed (In re Reed)*, 89 B.R. 100 (Bankr. C.D. Cal. 1988) (holding that under California law, bankruptcy trustee could not take advantage of presumption intended only for spouses at divorce that asset held in joint tenancy is community property for purposes of property division), *aff'd*, 940 F.2d 1317 (9th Cir. 1991). The presumption that all obligations are incurred in the interest of the marriage or the family, Wis. Stat. § 766.55(1), tends to make all marital property assets "liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse," 11 U.S.C. § 541(a)(2)(B); see also Wis. Stat. § 766.55(2)(b). If any of the marital property assets held by the nondebtor are includible in the estate under 11 U.S.C. § 541(a)(2)(B) and the value of these assets exceeds the amount necessary to satisfy claims, the assets may be returned to the nondebtor after claims are filed and the amount of excess is determined. The return of these assets might be by abandonment by the trustee or by court order upon motion by the nondebtor spouse.

Although nonexempt marital property assets held by a nonincurring and nonobligated spouse may be recovered by a creditor to satisfy a family-purpose obligation under section 766.55(2)(b), certain marital property assets held by the nondebtor spouse in the bankruptcy context might not be liable to any "extent" for a claim against the debtor or a claim against both the debtor and the debtor's spouse if the assets themselves are exempt under state law. Even though a nondebtor spouse is not entitled to exemptions under bankruptcy law, state law exemptions affect the extent of recovery under state law and hence, whether those assets are includible in the debtor's estate under 11 U.S.C. § 541(a)(2)(B). See Wis. Stat. § 815.18(3). For example, an IRA held

by the nondebtor spouse could not be recovered by a creditor because of the exemption under section 815.18(3)(j)1. and thus would not be includible in the debtor's estate.

An immediate practical concern to the trustee or debtor-in-possession is when to take possession of 11 U.S.C. § 541(a)(2)(B) assets and when the assets' inclusion in the estate is determined. Section 541 of the Bankruptcy Code does not indicate at what point in the bankruptcy proceeding the "extent" of includible assets held by the nondebtor spouse is determined, although it appears to be at the time of filing. 11 U.S.C. § 541(a)(1). The initial inclusion of *all* marital property assets in the estate, subject to a motion by the debtor or the debtor's spouse that particular marital property assets are not includible under 11 U.S.C. § 541(a)(2)(B), is the most practical approach to bankruptcy administration of marital property assets. The bankruptcy estate is created as of the filing of the bankruptcy petition, although certain specifically enumerated assets may be added later (such as assets acquired by inheritance, life insurance proceeds, or property settlement with the debtor's spouse, that the debtor acquires or becomes entitled to within 180 days of filing, 11 U.S.C. § 541(a)(5)). Income on estate property, 11 U.S.C. § 541(a)(6), transfers recovered by the trustee, 11 U.S.C. § 541(a)(4), and certain assets acquired after the date of filing are also added when the estate's interest arises. 11 U.S.C. § 541(a)(7). It would be contrary to 11 U.S.C. § 541(a)(1) to determine property of the estate at a date after filing, such as when claims are filed. Furthermore, the trustee or debtor-in-possession must expeditiously administer the estate; this is not feasible if it is not known until after the claims are filed whether a business or other asset that is classified as marital property and that is held by the nonfiling spouse will be in the estate. *See* 11 U.S.C. §§ 704, 1106. There are no Bankruptcy Code provisions outlining the trustee's duties with respect to the nondebtor spouse's marital property during the period between filing and the determination of claims. Therefore, if the property is not included in the estate as of the date of filing, the trustee would have no control or effective means of protecting the estate's interest. Since marital property business-related assets held by the nondebtor may be excluded after the administration of the estate has commenced, in many instances such a business should not be liquidated or even interrupted, especially if it is profitable. If the case is under Chapter 7, the trustee may wish to obtain an order authorizing continuation of operations. *See* 11 U.S.C. § 721.

It may under certain circumstances be possible to determine at the outset that there are no 11 U.S.C. § 541(a)(2)(B) assets in the estate. If all scheduled debts are predetermination date debts of the debtor, and if marital property assets held by the nondebtor spouse are traceable to the nondebtor spouse's wages or other marital property funds not subject to such obligations under Wisconsin law, *see* Wis. Stat. § 766.55(2)(c)1., then upon the nondebtor's motion, the assets could be excluded from the estate before any administration by the trustee. In that instance, marital property assets generated by the nondebtor would not be liable for any claim, and such property would not be includible under 11 U.S.C. § 541(a)(2)(B). *But see infra* § 6.105 (expanded rights of some categories of creditors to distributions from estate).

Another approach to determining property of the estate under 11 U.S.C. § 541(a)(2)(B) is to exclude the marital property assets held by the nondebtor, but to order payment to the estate of an amount determined to be necessary to pay qualified claims up to the net value of such assets. The amount would be determined after all claims are filed. This approach has been described as the equivalent of a "charging order," under which the trustee may call on the marital property assets held by the nondebtor only if other assets includible in the estate are insufficient to pay all allowable claims. *See Pedlar, supra*, at 360. Arguably, excluded business interests classified as community (marital) property, such as a sole proprietorship, should be "charged" only to the extent the value of the assets exceeds business debts. *See id.* In other words, the amount of the net value of the proprietorship would be paid into the estate, but the assets themselves would not be under the trustee's control. Such a charging order might be equitable in some circumstances, but it does not appear to be available under the language of 11 U.S.C. § 541(a)(2)(B). The order would mean that a sole proprietorship that is classified as marital property and held by the nondebtor spouse, and in which the nondebtor spouse is employed, would no longer be treated differently from a closely held corporation, the stock of which is classified as marital property, held by the nondebtor spouse and in which the nondebtor spouse is employed. With a sole proprietorship, the estate includes the business assets, with the result that personal and business creditors are in the same class and have equal priority; with a corporation, the estate includes only the nondebtor spouse's stock, with the result that the business creditors have first rights to recover from the business assets.



The following example illustrates possible consequences of the disparity in treatment that results if a business classified as marital property in which the nondebtor spouse is active is a sole proprietorship rather than a corporation.

➤ *Example.* Assume a debtor has \$10,000 in unsecured debts and all other assets are exempt. The nondebtor nonfiling spouse holds a sole proprietorship that is classified as marital property, and assets used in the business are worth \$10,000. There are business-related unsecured debts of \$12,000. The bankruptcy estate of the spouse who is not active in the business consists of the \$10,000 in nonexempt business-related assets and total claims of \$22,000. These creditors are paid pro rata at the rate of about 45% (\$10,000 is used to pay \$22,000 in claims). On the other hand, if the business were held in corporate form by the nondebtor spouse, the stock's fair market value in the estate would presumably be zero. Since under that assumption there would be no value in the estate, the trustee would abandon the stock. If the business were later liquidated, the unsecured business creditors would receive about 83% of their claims (\$10,000 would be used to pay \$12,000 in claims), and the creditors holding obligations incurred by the debtor would receive nothing.

If the debtor's debts are secured, different consequences arise from the disparity in treatment, as illustrated in the following example:

➤ *Example.* Assume the same assets as in the previous example, except that the debtor has incurred priority debts of \$10,000 (such as taxes or other priority debts under 11 U.S.C. § 507) rather than unsecured debts lacking priority status. The priority debts are paid in full before any unsecured claims are allowed. In this example, the business creditors of a sole proprietorship classified as marital property and held by the nondebtor spouse receive nothing, and all the business assets are used to pay the priority claims incurred by the debtor spouse. Since the nondebtor spouse has not joined in the bankruptcy and remains personally liable to the business creditors, his or her nonmarital property, if any, may be reached to satisfy obligations to these business creditors. As in the previous example, if the nondebtor spouse's business were incorporated, it would be abandoned by the trustee, and business creditors would be able to recover from business assets.

See Alan Pedlar, *The Implications of the New Community Property Laws for Creditors' Remedies in Bankruptcy*, 63 Cal. L. Rev. 1610, 1631 (1975); see also *U.S. West Fin. Servs., Inc. v. Berlin (In re Berlin)*, 151 B.R. 719 (Bankr. W.D. Pa. 1993); *In re Lundell Farms*, 86 B.R. 582, 590–91 (Bankr. W.D. Wis. 1988) (holding that even though partnership interests were classified as marital property, asset owned by debtor partnership was not classified as marital property because it was owned by partnership and not by married partners; therefore, any application of marital property principles was inappropriate).

Whereas community property is included in the bankruptcy estate of either spouse, only the debtor's interest in property owned in joint tenancy is included in his or her estate. Assets titled in joint tenancy and tenancy in common after the determination date exclusively between spouses are included in the estate of one spouse since, absent a marital property agreement or contrary intent of the asset's donor, attempts to title assets using these forms of ownership result in marital property or survivorship marital property. Wis. Stat. § 766.60(4)(b). In other community property states, the form of title may give rise to a presumption as to whether property titled in the spouses' names as joint tenants is treated as community property or as a true joint tenancy. See, e.g., *Rhoads v. Jordan (In re Rhoads)*, 130 B.R. 565 (Bankr. C.D. Cal. 1991) (holding that under California law, persons who hold property titled in joint tenancy are presumed to own asset as joint tenants and asset is not considered community property); *Swink v. Sunwest Bank (In re Fingado)*, 113 B.R. 37 (Bankr. D.N.M. 1990) (holding that assets held in joint tenancy presumed to be community property under New Mexico law); see also Sommer & McGarity, *supra* § 6.6, ¶ 4.01, at 4–5. A presumption created by title can be rebutted, resulting in the inclusion or exclusion of the nondebtor's one-half interest in an asset, depending on the proof of the parties' intent as to their ownership interests.

In contrast to the rules in other community property states, section 766.60(4)(a) states that

Except as provided in par. (b) . . . to the extent the incidents of the tenancy in common or joint tenancy conflict with or differ from the incidents of property classification under this chapter, the incidents of the tenancy in common or of the joint tenancy, including the incident of survivorship, control.

This rule applies to all assets that are owned in joint tenancy by a spouse and acquired before or after the determination date. It is a rule of law, not a presumption. The paragraph (b) referred to in the quoted material states that if a document of title, instrument of transfer, or bill of sale expresses an intent to create a joint tenancy, the asset is survivorship marital property, and if the intent was to create a tenancy in common, the asset is marital property. Wis. Stat. § 766.60(4)(b). That paragraph applies to assets, other than bank accounts governed by chapter 705, that are acquired exclusively between spouses after the determination date and are titled in the spouses' names as joint tenants or as tenants in common.

If a particular asset to which section 766.60(4)(a) applies—that is, an asset held by the debtor and the debtor's spouse as joint tenants or tenants in common—was acquired before the determination date, part of the value of the asset may have become marital property as a result of the reduction of indebtedness with marital property funds or the application of substantial uncompensated labor that results in substantial appreciation. *See* Wis. Stat. § 766.63. In those circumstances, to argue that only the debtor's one-half interest in the asset is property of the estate would appear to conflict with 11 U.S.C. § 541(a)(2)(A), which makes all community property under the debtor's sole, equal, or joint management and control property of the estate. Even though, in some circumstances, rules relating to the disposition of assets held in joint tenancy exclusively between spouses will supersede rules relating to marital property classification, this does not prevent a component of the value from being classified as marital property. Therefore, it appears that if a fractional interest of an asset held in joint tenancy is classified as marital property, that interest is property of a debtor spouse's bankruptcy estate. 11 U.S.C. § 541(a)(2)(A); *see infra* § 6.78 (management and control of assets co-owned by bankruptcy trustee and another party).

An asset to which section 766.60(4)(b) applies—that is, an asset acquired after the determination date and titled exclusively in the names of both spouses as joint tenants or tenants in common—will be in the estate of either spouse since both marital property and survivorship marital property assets held by both spouses are in the bankruptcy estate of either spouse under 11 U.S.C. § 541(a)(2)(A). This is true even if the asset was acquired with property or funds of another classification. *See also supra* ch. 2.

Section 766.70 makes clear that interspousal remedies are available only to the other spouse, not to a third party such as a creditor. *See* Wis. Stat. Ann. § 766.70 Legis. Council Notes—1985 Act 37, §§ 89, 130 to 138 (West 2009). Therefore, it appears that an interspousal remedy to which one spouse is entitled does not become property of the estate of the spouse entitled to a remedy.

The fact that an asset is subject to community claims does not mean that the asset is included in property of the estate under 11 U.S.C. § 541(a)(2)(B) unless it is also community property. In *Anderson v. Conine (In re Robertson)*, 203 F.3d 855 (5th Cir. 2000), the debtor and his former wife were divorced, and their community property was partitioned pursuant to Louisiana law before the husband filed his Chapter 7 case. The Fifth Circuit Court of Appeals held that the trustee could not set aside the partition that made the debtor's former homestead the separate property of his former wife because the partition was constructive notice to a hypothetical bona fide purchaser. Furthermore, the fact that the former wife and her property might have been subject to actions to recover community debts did not mean that her property was community property, and her separate-property house was not property of the debtor's estate.

In *Brassett v. Brassett (In re Brassett)*, 332 B.R. 748 (Bankr. M.D. La. 2005), a former wife filed a bankruptcy petition after the effective date of her divorce but before the couple's community property was partitioned. Under Louisiana law, no further community property was acquired after the divorce. Under bankruptcy law, all community property becomes part of the bankruptcy estate when one spouse files a bankruptcy petition, and unpartitioned community property after divorce is treated in the same manner. *See* 11 U.S.C. § 541(a)(2). The nonfiling former husband argued that postdivorce distributions that he received from a community property joint venture were earned income, which would have been his separate property, but the court held that these were equity distributions of a community property business. Accordingly, those distributions became part of the wife's bankruptcy estate, and her right to an accounting of them and to recovery of her share in them also passed to her estate.

### (3) Future Income [§ 6.77]

Under section 541(a)(6) of the Bankruptcy Code, earnings received for postpetition services performed by the debtor are not property of the estate of a Chapter 7 or Chapter 11 debtor. A debtor may voluntarily submit those earnings to fund a Chapter 11 plan. The postpetition earnings of the spouse of a Chapter 7 or Chapter 11 debtor are not included in 11 U.S.C. § 541 and therefore also are not property of the estate. *See* 11 U.S.C. § 541(a)(6).

Sections 1207(a)(2) and 1306(a)(2) of the Bankruptcy Code contain exceptions to 11 U.S.C. § 541(a)(6) in that earnings for services performed by the debtor between the filing of the petition and the completion of the Chapter 12 or 13 plan, at least to the extent needed to fund the plan, are included in the estate. The debtor's "future income" is submitted to the control and supervision of the Chapter 12 or 13 trustee. 11 U.S.C. §§ 1222(a)(1), 1322(a)(1). Earnings of the nondebtor spouse are generally not subject to provisions in a Chapter 12 or 13 plan, even though they are marital property.

In *In re Reiter*, 126 B.R. 961 (Bankr. W.D. Tex. 1991), however, the court held that the nondebtor spouse's wages were property of the estate under 11 U.S.C. § 1306(a)(1) because they were community property described in 11 U.S.C. § 541(a)(2) and because the debtor acquired an interest in those wages after commencement of the case. Before a plan was confirmed, the automatic stay applied to the nondebtor spouse's wages as property of the estate, 11 U.S.C. § 362(a)(2), to prevent the IRS from recovering the debtor's interest in those wages and to limit the IRS to a claim in the estate.

➤ **Comment.** It is arguable, based on the reasoning in *Reiter*, that the debtor's marital property interest in the earnings of the nonfiling spouse is "future income of the debtor" that is required to be submitted to the control of the Chapter 12 or 13 trustee. *See* 11 U.S.C. §§ 1222(a)(1), 1322(a)(1). *But see In re Nahat*, 278 B.R. 108 (Bankr. N.D. Tex. 2002) (holding that nondebtor spouse's community property earned income is a "special" type of community property under Texas law and is not property of estate because it is under sole management and control of the nondebtor spouse and is not subject to claims against the debtor); *In re Markowicz*, 150 B.R. 461 (Bankr. D. Nev. 1993) (holding that after confirmation of plan, nondebtor

spouse's income was not property of estate). However, it appears that there have been no cases in which a Chapter 13 trustee has attempted or been able to have part of a nondebtor spouse's wages paid into the plan without that spouse's consent. The benefit of the nondebtor spouse's earnings to the debtor may, nevertheless, affect the determination of whether the debtor's disposable income is subject to the plan and whether the plan is proposed in good faith. 11 U.S.C. §§ 1225(a)(3), (b)(2), 1325(a)(3), (b)(2); *In re Bottleberghe*, 253 B.R. 256 (Bankr. D. Minn. 2000); *In re Enret*, 238 B.R. 85, 88 (Bankr. D. N.J. 1999); *In re Soper*, 152 B.R. 985 (Bankr. D. Kan. 1993); *In re Belt*, 106 B.R. 553 (Bankr. N.D. Ind. 1989); *In re Saunders*, 60 B.R. 187 (Bankr. N.D. Ohio 1986). If the nondebtor spouse's earnings are available to meet the debtor's expenses, the plan will not be confirmed unless these wages are taken into consideration. *In re Belt*, 106 B.R. 553; *In re Saunders*, 60 B.R. 187.

#### **d. Management and Control by Trustee or Debtor-in-possession [§ 6.78]**

Upon the filing of a bankruptcy petition, the Chapter 7 trustee or the debtor-in-possession under Chapters 11, 12, or 13, as the case may be, obtains management and control of all property of the estate. 11 U.S.C. §§ 704, 1107(a), 1203, 1303; *see also* 4 *Collier, supra* § 6.72, ¶ 541.15. As it appears from the discussion in sections 6.74–.77, *supra*, all marital property assets may be in the debtor's estate, including all business-related marital property (described in section 766.70(3)(a)–(d)) held by the nondebtor spouse, even though those assets are not under the debtor's management and control at the time of filing. Although a spouse who does not hold a business interest classified as marital property and described in section 766.70(3)(a)–(d) cannot achieve management and control of the asset under Wisconsin law, *see* Wis. Stat. §§ 766.51(1)(am), .70(3), (4), the Bankruptcy Code supersedes state law and appears to authorize such a transfer of management and control. 4 *Collier, supra* § 6.72, ¶ 541.15. Therefore, any marital property business interest becomes subject to the management and control of the Chapter 7 trustee or the spouse who filed under Chapter 11, 12, or 13, whether or not that spouse held the business interest before the bankruptcy petition was filed. If necessary, the debtor-in-possession or trustee may compel transfer of the estate's property. 11 U.S.C. § 542.

See also *In re Brassett*, 332 B.R. 748 (Bankr. M.D. La. 2005) (holding that debtor spouse's right to recover community property interest in postdivorce unpartitioned asset passed to her bankruptcy estate); *supra* § 6.76.

➤ **Comment.** The practical result of the above rule is that a spouse unable to achieve management and control under state law may be able to do so by invoking bankruptcy law.

If property of the estate is held by a spouse and a third party, the trustee or debtor-in-possession may under certain conditions sell both the estate's and the co-owner's interest in the property. 11 U.S.C. § 363(h). Section 363(h) of the Bankruptcy Code provides that if the asset is owned by the debtor and a nondebtor party as joint tenants or as tenants in common, the trustee may sell the entire asset, provided that (1) partition in kind is impracticable; (2) the estate's share will be greater than would be realized by the sale of a fractional interest; (3) the benefit to the estate outweighs the detriment to the co-owner, including consideration of noneconomic interests; and (4) the asset is not used in the production of certain types of energy. 11 U.S.C. § 363(h); *see, e.g., Sapir v. Sartorius*, 230 B.R. 650 (S.D.N.Y. 1999), *aff'd*, No. 99-5020, 2000 WL 234456 (2d Cir. Feb. 1, 2000) (unpublished opinion); *Gazes v. Roswick (In re Roswick)*, 231 B.R. 843 (Bankr. S.D.N.Y. 1999); *Bakst v. Griffin (In re Griffin)*, 123 B.R. 933 (Bankr. S.D. Fla. 1991); *In re Waxman*, 128 B.R. 49 (Bankr. E.D.N.Y. 1991); *Greene v. Levenhar (In re Levenhar)*, 30 B.R. 976 (Bankr. E.D.N.Y. 1983); *Morris v. Ivey (In re Ivey)*, 10 B.R. 230 (Bankr. N.D. Ga. 1981).

These restrictions on the right to sell the entire asset do not apply to an asset formerly owned by the spouses as community property. 11 U.S.C. § 363(h); *In re Lang*, 191 B.R. at 272 (holding that federal bankruptcy law preempts Puerto Rican law that requires consent of both spouses for sale of community property); *Swink v. Sunwest Bank (In re Fingado)*, 995 F.2d 175 (10th Cir. 1993); *see also Kapila v. Morgan (In re Morgan)*, 286 B.R. 678 (Bankr. E.D. Wis. 2002).

If an asset is subject to sale in its entirety by the trustee, then the co-owner (in the case of an asset owned in joint tenancy, tenancy in common, or tenancy by the entireties) or the spouse (in the case of former community property) has the right to purchase the asset from the estate at the same price that would have been received from a third-party buyer. 11 U.S.C. § 363(i).

When the bankruptcy filing is for the sole purpose of gaining management and control over the nondebtor spouse's marital property assets, or when there is clear solvency and no legitimate reason for bankruptcy administration, the bankruptcy court may abstain from exercising jurisdiction after notice and hearing. *See* 28 U.S.C. § 1334(c); 11 U.S.C. § 305; *see also* 4 *Collier, supra* § 6.72, ¶ 541.15. Procedurally, the spouse holding a marital property asset, such as a business interest that is classified as marital property and that need not be brought into the estate under 11 U.S.C. § 541(a)(2)(B), may move to have the court abstain from exercising jurisdiction over the case. 11 U.S.C. § 305. Alternatively, the spouse may move the court for an order requiring that the trustee abandon the property if it would be of inconsequential value or benefit to the estate, such as an asset that has a small marital property component and is primarily the nonmarital property of the nonfiling spouse. 11 U.S.C. § 554(b); *see also Ludwig v. Geise (In re Geise)*, 132 B.R. 908 (Bankr. E.D. Wis. 1991). Abstention, abandonment, or refusal by the court to order transfer of the asset to the trustee or debtor-in-possession effectively returns the property to the nondebtor who owns it or in whose name it is held.

**e. Classification of Property by Court Order,  
Marriage Agreement, Interspousal Gift, or  
Unilateral Statement [§ 6.79]**

**(1) In General [§ 6.80]**

Property may be classified by court order under section 766.70; future income on nonmarital property assets may be classified as individual property by execution of a unilateral statement under section 766.59; and property may be classified by a marital property agreement under section 766.58, by written consent relating to life insurance under section 766.61(3)(e), or by gift. *See* Wis. Stat. § 766.31(10). A property division in a dissolution action can also change the ownership of property. *See* Wis. Stat. § 767.61. Classification by court order or by voluntary action of one or both of the spouses may affect whether property is included in the estate under 11 U.S.C. § 541(a)(2) or is excluded because former marital property assets became the individual property assets of the nonfiling spouse.



## (2) Court Order [§ 6.81]

Subject to being set aside by the bankruptcy court as a fraudulent transfer, a state court decree may alter the classification of a spouse's property or govern the determination of property includible in a bankruptcy estate, as illustrated by *Britt v. Damson*, 334 F.2d 896 (9th Cir. 1964), a case involving a separation agreement incident to a dissolution under Washington law. The plaintiff in *Britt* was the trustee in bankruptcy for the defendant's former husband. The trustee sought to have the Washington divorce decree set aside any former community property brought back into the bankruptcy estate. His action was predicated on theories that (1) the trustee succeeded to the rights of a lien creditor (under 11 U.S.C. § 110(c) (1958), the predecessor statute to 11 U.S.C. § 544(a)); (2) the property division was a fraudulent conveyance under state law (under 11 U.S.C. § 110(e)(1) (1958), predecessor to 11 U.S.C. § 544(b)); and (3) the transfer rendered the debtor insolvent or with unreasonably small capital and was for insufficient consideration (under 11 U.S.C. § 107(d)(2) (1958), predecessor to 11 U.S.C. § 548(a)). The lower court ruled in the defendant's favor on the ground that her former husband had no right to subject her separate property to a bankruptcy proceeding. The Ninth Circuit Court of Appeals also ruled in the defendant's favor and analyzed the trustee's various theories, rejecting all of them.

The appellate court noted that a distinction must be made between the rights of a hypothetical lien creditor with respect to property of the estate and the rights of creditors under state law with respect to former community property in the hands of the nondebtor spouse. Hypothetical lien rights in bankruptcy extend only to property of the estate. The debtor had no interest in the property awarded to his former wife, and he could not bring that property into the estate. Therefore, the trustee as a hypothetical lien creditor had no rights in the property the former wife received in the division of property. *Britt*, 344 F.2d at 900. In contrast to a hypothetical lien creditor's rights, state creditors' rights are not necessarily diminished by the exclusion of former community or marital property assets from the bankruptcy estate when one of the former spouses files a bankruptcy petition after the marriage is dissolved. At the time *Britt* was decided, Washington law conferred rights on creditors in existence before a divorce, as does Wisconsin under section 766.55(2m), allowing those creditors whose rights attached before the divorce to proceed against former community property received by the nonincurring

spouse. The creditors whose rights arose before the dissolution may recover those assets under state law. *See* Wis. Stat. § 766.55(2m).

The *Britt* court analyzed the definition of the term *transfer* and determined that a transfer had taken place, but to the extent that community property had been divided equally there was fair consideration. *Britt*, 334 F.2d at 903. The amount recoverable by the trustee therefore would be any portion in excess of 50% of the community property received by the nondebtor spouse without sufficient consideration. Consideration might be an equitable factor and might include maintenance and child support provisions. If the division had been unequal, then a circuit court, not the appellate court, could determine whether consideration was fair and whether the debtor was rendered insolvent or with unreasonably small capital. *Id.* at 902. This case made no distinction between a court order reached by stipulation and one reached by contested proceedings, but that may be a relevant factor in determining fair consideration.

➤ **Comment.** *Britt* has been criticized as allowing spouses to agree to remove property from the bankruptcy estate and to put property beyond creditors' reach. *See* 4 *Collier, supra* § 6.72 ¶ 541.15.

A court order under section 766.70 may also alter property classification, and such an order would determine the extent to which the spouses' property passes to the bankruptcy estate. An order under section 766.70 issued during an ongoing marriage would probably be analyzed in the same manner as outlined in *Britt* to determine whether a fraudulent conveyance occurred by reason of the order. *See supra* § 6.42 (Wisconsin creditor's rights without notice of court order under section 766.70).

### (3) Marriage Agreement [§ 6.82]

It appears that the terms of a marriage agreement are effective against a bankruptcy trustee, unless the effect of such an agreement is a voidable fraudulent transfer under 11 U.S.C. § 548(a) and (b) or 11 U.S.C. § 544(b). Determining property of the estate requires reference to state law to determine the debtor's rights in property, and if the debtor has no rights in property classified by agreement as the individual property of the nondebtor spouse, then the property is not included in the bankruptcy estate. *See* 11 U.S.C. § 541(a).

For example, in *Rinehart v. Meek (In re Grady)*, 128 B.R. 462 (Bankr. E.D. Wis. 1991), the court held that an opt-out agreement between the debtor and his wife, entered into after marriage and immediately before the effective date of the Act, was binding on the bankruptcy trustee. The classifications established in the agreement were followed in determining the property division at the time of the couple's divorce, which occurred before the former husband's bankruptcy. Some of the assets the wife received in the dissolution would have been classified as marital property absent the agreement, but pursuant to the agreement, the assets were her individual property when acquired. Even though the former wife received substantially more assets in the property division than did the debtor, she had acquired most of them from her family by gift or inheritance. She received only her own property in the property division. Thus, since the property division at divorce did not effectuate a transfer, it could not be a fraudulent transfer that was avoidable by the trustee.

Similarly, the bankruptcy court in *Geise*, 132 B.R. 908, held that a statutory individual property classification agreement (SIPCA), signed by a debtor and his spouse after their marriage and after the Act was in effect, was binding on the bankruptcy trustee. The nondebtor spouse was entitled to trace her individual property assets as determined under the SIPCA, including a portion of the value of a house that had become mixed property. Assets classified as individual property by the SIPCA retained their individual property classification even after the SIPCA expired. Only the component part of the mixed property house that was classified as marital property was property of the estate and subject to transfer to the trustee; however, the marital property component of the value of the nondebtor's house was so small that payment was not required.

The court in *Pietri v. Pietri (In re Pietri)*, 59 B.R. 68 (Bankr. M.D. La. 1986), determined that a debtor's interest in the continuation of the Louisiana community property regime was not a property right or interest. Therefore, the recording of a prenuptial agreement in which each spouse gave up any right to future acquisition of community property and agreed to live under a separate property regime did not per se constitute a fraudulent transfer under 11 U.S.C. § 548. In Louisiana, a marital agreement is not effective as to third parties until it is recorded. In this case, the debtor failed to record the agreement until three years after the marriage and two weeks before the bankruptcy. The case was decided on summary judgment, and the court left open whether a

fraudulent transfer had actually occurred. It appears that the property accumulated before the agreement was recorded was community property as to the trustee, although the court refused to make a finding as to the trustee's rights in specific assets or the trustee's right to avoid transfers made by the debtor. *But see Rooz v. Kimmel (In re Kimmel)*, 367 B.R. 166 (Bankr. N.D. Cal), *aff'd*, 378 B.R. 630 (B.A.P. 9th Cir. 2007), *aff'd*, 302 Fed Appx. 518 (9th Cir. 2008), *cert. denied*, 129 S. Ct. 2394 (2009) (holding that such an agreement may be a fraudulent transfer under California law).

In an unpublished decision, the U.S. District Court in *In re Pappas*, No. 89-C-211-S (W.D. Wis. May 10, 1989), also found that a spouse does not have a present property interest in future accumulations of marital property and hence that forgoing those future accumulations does not constitute consideration. Consequently, a marital property agreement classifying those future rights did not constitute a transfer within the meaning of 11 U.S.C. § 548. It could not, then, be a fraudulent transfer, which the trustee under 11 U.S.C. § 548 could set aside, recovering the transferred assets for the estate. What this means is that a marital property agreement giving up any marital property interest in future acquisitions of property will be effective in keeping out of the debtor spouse's bankruptcy estate property acquired by the nondebtor spouse after the date of the agreement. The court contrasted the relinquishment of the future acquisition of a marital property interest with the relinquishment of a present support right. Forgoing a present right to support would constitute valuable consideration, for which there must be sufficient consideration in return. The agreement in *Pappas* had included a provision requiring the husband to transfer to the wife stock in his family business—that is, requiring the husband to forgo a present right. The husband argued that the motivation for the transfer was to promote “marital harmony.” The court found that marital harmony did not constitute “value.” Therefore, the transfer had been for no consideration, and the trustee could avoid the transfer and recover the stock for the estate. *See also Zubrod v. Kelsey (In re Kelsey)*, 270 B.R. 776, 781 (B.A.P. 10th Cir. 2001) (“Value is not measured from the subjective, emotional perspective of Mr. Kelsey, but instead from the objective, economic prospective of his creditors”).

Under section 766.55(4m), any of the debtor's creditors who are without actual knowledge or notice of the agreement may recover from the transferee spouse property that would have been available to the creditor but for the agreement. In addition, creditors are entitled to

proceed under section 766.55(4m) against former marital property assets that are classified as the nondebtor's individual property if the obligation was incurred before the execution of the agreement that reclassified such property as the nondebtor spouse's individual property. Therefore, in Wisconsin the rights of these two sorts of creditors are not adversely affected by excluding from the bankruptcy estate assets that would have been in the estate but for the agreement. The creditor may seek recovery against the nondebtor transferee spouse in state court, notwithstanding the effect of the discharge, because nonmarital property owned by the transferee is not protected by the discharge. *See infra* §§ 6.106–.110. Such creditors may be in a better position to recover than if the reclassified property were in the bankruptcy estate. If such property were in the estate, it would be subject to priority claims and other community claims against the debtor or both the debtor and the debtor's spouse, as well as to the claim of the creditor who had no notice of the agreement or court order. *See infra* §§ 6.92–.104.

The very existence of the creditor who had no notice, however, may enable the trustee to bring the reclassified property into the estate. Notwithstanding the general principle that a marriage agreement is binding on the trustee, the trustee may have avoidance powers, other than the power to set aside a fraudulent conveyance, that might bring assets into the estate that would otherwise be excluded by the agreement. These include powers as a hypothetical judicial lien creditor, a hypothetical execution creditor whose execution was returned unsatisfied, and a hypothetical bona fide purchaser, all as of the date of filing the petition. 11 U.S.C. § 544(a). Although these powers would probably not permit the trustee to set aside the marital property agreement, the trustee may invoke the power of 11 U.S.C. § 544(b) to set aside the agreement if there is an actual creditor who did not receive a copy or had no actual knowledge of the agreement before granting credit.

The trustee's powers as hypothetical creditor, executor, or purchaser allow the trustee to recover property from a transferee or third party for the benefit of the estate. 11 U.S.C. §§ 544(a), 550. The hypothetical creditor, however, arguably does not extend to include the creditor who has the right to set aside the agreement and recover property that would have been property of the estate absent the agreement. That creditor is only a creditor who had no actual knowledge of the agreement or did not receive a copy. It is not totally clear that a hypothetical creditor or purchaser would be deemed to have notice of a marital property agreement, but the better view would appear to be that the hypothetical

creditor or purchaser would be deemed to have notice. Otherwise, an agreement would not bind the trustee, regardless of how conscientious the debtor was in disclosing the agreement to creditors.

On the other hand, 11 U.S.C. § 544(b) states that the trustee can avoid a transfer that is voidable by an actual existing creditor who has an allowable claim because the creditor had no notice or knowledge of the agreement. The trustee in *Geise*, 132 B.R. at 913, had argued that because none of the creditors had been given notice of or a copy of the SIPCA before granting credit, he should be able to exercise the rights of such a creditor and not be bound by the agreement. 11 U.S.C. § 544(b). However, it appears that, except for the debt to the DOR, all the debtor's obligations were incurred before the agreement was entered into. *See* Wis. Stat. § 71.10(6)(a). The DOR is not a creditor as defined by section 766.01(2r) nor does it "extend credit." *Geise*, 132 B.R. at 913. Consequently, because there were no creditors entitled to avoid the agreement under state law, the trustee was not able to exercise the rights of such a creditor. *See* 11 U.S.C. § 544(b).

Section 766.55(4m) states that if a creditor does not receive a copy of an agreement or a court decree under section 766.70, the agreement cannot adversely affect the creditor, unless the creditor has actual knowledge of the adverse provision. The section does not say that the agreement is void. It is arguable that if the creditor's remedies were sufficient for it to recover in spite of the agreement, the creditor would be bound by terms of the agreement. It is also arguable that anything that diminishes the assets available for recovery constitutes an "adverse effect." If the creditor's ability to recover the nondebtor spouse's assets were adversely affected because of the manner in which the agreement classified property, and if this result were interpreted to make the agreement void as to that creditor, then the trustee could avoid the agreement and bring into the bankruptcy estate property that would have been marital property absent the agreement. Bringing the assets into the estate benefits all creditors, not solely the creditor without notice of the agreement.

One effect of bankruptcy is that an executory contract, described generally as one in which obligations remain to be performed on both sides, may be rejected or, under certain circumstances, assumed and assigned. *See* 11 U.S.C. § 365. The individual Chapter 11 debtor in *In re Draper*, 790 F.2d 52 (8th Cir. 1986), attempted to reject his marital settlement agreement as an executory contract under 11 U.S.C. § 365.

The bankruptcy court denied the debtor's motion, finding that his obligation to provide for his children's college education was actually in the nature of a support obligation rather than an executory contract. The district court and the court of appeals affirmed this view as not being clearly erroneous. The court of appeals noted that even if the agreement had been rejected, the damages for the breach would have been nondischargeable support, providing the same result as denying rejection of the agreement.

#### **(4) Gift [§ 6.83]**

Property may be reclassified by a gift between spouses, which also reclassifies the income from that property as the individual property of the donee spouse (unless the donor spouse provides otherwise). Wis. Stat. § 766.31(10). Section 766.55(4m)—which provides that a creditor without actual knowledge or without a copy of a marital property agreement or a decree under section 766.70 cannot be adversely affected by a provision of the agreement or decree—does not apply to gifts. Therefore, a gift that reclassifies marital or nonmarital property of the obligated donor as the individual property of the nonobligated donee is generally binding on the creditor. Creditors cannot avoid the transaction in the same manner that they can if the reclassification was by decree or agreement. *See* Wis. Stat. § 766.55(4m); *see also supra* § 6.37. However, if a transfer could have been avoided by a creditor as a fraudulent transfer, it can also be avoided by the bankruptcy trustee and brought into the estate. *See* 11 U.S.C. §§ 544(b), 548.

#### **(5) Unilateral Statement [§ 6.84]**

Under section 766.59, a spouse may execute a statement that classifies the income on that spouse's nonmarital property assets as individual property. Without the statement, such income is classified as marital property. Wis. Stat. § 766.31(4). It is not clear whether a unilateral statement by a nondebtor spouse will be effective to exclude accumulations of such income from the bankruptcy estate of the debtor spouse.

One possible view is that for some purposes under state law, Wis. Stat. § 766.59(5), a unilateral statement is treated like a contract and the authority of state contract law to determine the rights of individuals is

well recognized under federal law. However, a unilateral statement is not a contract. The adverse interests of contracting parties and litigants are more likely than a unilateral act to protect the spouses' rights in property, including property that is included in the bankruptcy estate, and this will also protect the rights of the spouses' creditors. In addition, the unilateral withdrawal by one spouse of income from the pool of marital property is sufficiently dissimilar from agreements and court orders that arguably it need not be recognized by federal law. The income from the nonfiling spouse's nonmarital property would then be in the estate of the debtor spouse, notwithstanding the nonfiling spouse's unilateral statement.

A better view is to classify such income as the individual property of the nondebtor spouse and to exclude it from the debtor's estate. Income subject to the unilateral statement is not marital property under state law, Wis. Stat. § 766.31(7p), and so is not includible in the estate as marital property under 11 U.S.C. § 541(a)(2). Furthermore, creditors of the debtor spouse are protected under state law if they had no notice of the unilateral statement, because they may recover property held by the nonincurring spouse that would have been marital property absent the statement. *See* Wis. Stat. §§ 766.55(4m), .59(5). Creditors of the debtor spouse who had notice of the nondebtor spouse's election are bound by its terms, which is fair in light of the notice before the granting of credit. However, if the trustee may set aside a marital property agreement using one of the trustee's avoidance powers, a unilateral statement should also be subject to avoidance. *See supra* § 6.82.

## **f. Voidable Transfers [§ 6.85]**

### **(1) In General [§ 6.86]**

Property of a bankruptcy estate includes property recovered by a bankruptcy trustee under the trustee's powers to avoid (nullify) certain transfers made before the filing of the bankruptcy petition. 11 U.S.C. § 541(a)(3). These voidable transfers include:

1. Transfers to a "custodian" under 11 U.S.C. § 542 (such as a receiver, sheriff after levy, or other party holding a nonbeneficial interest);



2. Fraudulent transfers or gifts that could have been avoided by a creditor under state law, 11 U.S.C. § 544(b), or under 11 U.S.C. § 548;
3. Set-offs, 11 U.S.C. § 553;
4. Property acquired on account of a bankruptcy trustee's other special lien avoidance powers, 11 U.S.C. §§ 544, 545, 724(a);
5. Excessive payments to an attorney, 11 U.S.C. § 329(b);
6. Recovery from general partners of a debtor partnership, 11 U.S.C. § 723; and
7. Preferences, 11 U.S.C. § 547.

*See generally* 11 U.S.C. §§ 541(a)(3), (4), 550. The trustee may also avoid certain postpetition transfers and collusive sales. 11 U.S.C. §§ 549, 363(n). The most common types of avoidable transfers are preferences under 11 U.S.C. § 547, fraudulent conveyances under 11 U.S.C. §§ 548 and 544(b), and transfers subject to the trustee's avoidance powers as a hypothetical creditor or bona fide purchaser under 11 U.S.C. § 544(a). *See supra* § 6.82 (trustee's avoidance powers under 11 U.S.C. §§ 544 and 548 with respect to marriage agreements).

If the trustee avoids a transfer, thereby bringing an asset into the estate, the debtor may claim the asset exempt, provided that the asset qualifies for an exemption, the transfer was not voluntary, and the debtor did not conceal the property. 11 U.S.C. § 522(g). If the trustee chooses not to avoid a transfer, usually because the debtor is entitled to claim it exempt under 11 U.S.C. § 522(g), the debtor may use the trustee's avoidance powers to recover the asset. 11 U.S.C. § 522(h). The debtor may also be entitled to avoid nonpossessory, non-purchase money liens on certain exempt assets and to avoid judicial liens unrelated to support of dependents to the extent those liens impair an exemption. 11 U.S.C. § 522(f).

## **(2) Preferences [§ 6.87]**

A preference under 11 U.S.C. § 547 is a transfer of a debtor's property (which includes the debtor's interest in marital property assets)

to or for the benefit of a creditor in payment of a debt in existence at the time of payment. To be avoidable, the transfer must have been made while the debtor was insolvent and must have resulted in the creditor's receiving more than the creditor would have received under Chapter 7 if the transfer had not been made. 11 U.S.C. § 547(b). Transfers may be avoided as preferences if they are made (1) on or within 90 days before the filing of the bankruptcy petition, if the transfer was to an ordinary creditor, or (2) within one year before the filing if the transfer was to an "insider" (defined in 11 U.S.C. § 101(31)). 11 U.S.C. § 547(b)(4). A debtor is presumed to be insolvent within the 90 days before filing. 11 U.S.C. § 547(f). Certain defenses are available to transferees; for example, avoidance is not permitted in the case of transfers that occur for new or contemporaneous consideration or in the ordinary course of business. 11 U.S.C. § 547(c).

A transfer of marital property assets by a nondebtor spouse in connection with a debt incurred by either spouse may also be a preference. *See* Pedlar, *supra*, § 6.76, at 372.

➤ **Example.** Assume that a farmer who is a sole proprietor uses marital property funds to pay a seed company for an antecedent debt incurred in operating the farm. The farmer's spouse files a petition in bankruptcy within 90 days after the payment. The spouse's trustee may recover the payment from the seed company as a preference. *See also infra* § 6.105 (administration of assets recovered by avoided transfers in bankruptcy estate).

A preference is a transfer that, among other things, was made to a creditor for an antecedent debt—that is, a payment that is not a contemporaneous exchange for consideration. The term *creditor* is defined in 11 U.S.C. § 101(10)(c) to include an entity holding a *community claim*, a term defined in 11 U.S.C. § 101(7). Since it appears that all categories of obligations under section 766.55(2) are community claims, *see infra* §§ 6.92–.104, with disallowance under certain circumstances, then almost any payment on an antecedent obligation by either spouse with marital property funds or with the debtor's nonmarital property funds during the preference time period is voidable. *See* Pedlar, *supra* § 6.76, at 386–88; 4 *Collier, supra* § 6.72, ¶ 547.05.

To constitute an avoidable preference, a transfer must have occurred while the debtor was insolvent. 11 U.S.C. § 547(b)(3). Whether the debtor was insolvent at the time of the transfer is determined by

reference to the definition of the term *insolvent* in 11 U.S.C. § 101(32). The definition states that a debtor is insolvent when “the sum of such entity’s debts is greater than all of such entity’s property,” exclusive of certain exceptions. 11 U.S.C. § 101(32). *Debt* means liability on a claim, 11 U.S.C. § 101(12), and a claim includes a “claim against property of the debtor,” 11 U.S.C. § 102(2). One commentator has stated that an “entity’s debts” should be read to mean “community claims.” Pedlar, *supra* § 6.76, at 387. Such a reading is logical but apparently incorrect because a literal reading of the relevant statutes does not lead to the definition of community claim in 11 U.S.C. § 101(7). *See* 11 U.S.C. §§ 101(12), (5), 102(2). Therefore, even though all obligations under section 766.55(2) are included within the definition of community claim, 11 U.S.C. § 101(7); *see infra* §§ 6.92–.104, for the purpose of distributing the estate, only obligations meeting the definition of *claim against property of the debtor* are used in determining insolvency.

In determining insolvency, the classification of property actually included in the bankruptcy estate and the availability of property under section 766.55(2) may be important. Obligations can meet the definition of community claim whether or not property exists that is available to satisfy such obligations under state law. 11 U.S.C. § 101(7); *see infra* §§ 6.95–.104. However, the definition of claim against property of the debtor depends on the nature of the obligation and the classification of property actually in the estate. If marital property assets in the estate are available to satisfy the category of debt under section 766.55(2)(c)–(d), then the creditor has a claim against the debtor’s property. 11 U.S.C. § 102(2); *see infra* § 6.94.

The following example illustrates the difference between a community claim and a claim against the debtor’s property.

➤ **Example.** Assume that the estate consists of marital property assets owned by the debtor and the debtor’s nonfiling spouse that are traceable only to the debtor’s earnings. The premarriage creditor of the debtor’s spouse has a community claim because there could conceivably have been marital property assets in the estate that were traceable to the earnings of the nondebtor spouse. Wis. Stat. § 766.55(2)(c)1. However, because the estate does not actually contain such assets, the creditor does not have a claim against the debtor’s property. The obligation, therefore, is not included in measuring the debtor’s insolvency under 11 U.S.C. § 547(b)(3).

because it is not a claim against the debtor's property and hence is not one of the "entity's debts" under 11 U.S.C. § 101(32).

➤ **Example.** A tort or nonfamily-purpose obligation of the nonfiling spouse is collectible only from the nondebtor's one-half of marital property. Such an obligation would not be counted to determine insolvency since it is not a claim against the debtor's property and so is not part of the "entity's debts." Such appears to be the case, even though the trustee may be attempting to recover marital property funds transferred by the nondebtor in satisfaction of a tort or nonfamily-purpose obligation of that spouse.

Furthermore, the insolvency test measures the entity's debts against "such entity's property." 11 U.S.C. § 101(32). The term *entity* is defined to include a "person, estate, trust [and] governmental unit." 11 U.S.C. § 101(15). The entity's property is not necessarily synonymous with the bankruptcy estate determined under 11 U.S.C. § 541 because the estate may include the nondebtor spouse's interest in marital property as well as the debtor's. If only the debtor's property is used to measure insolvency, only one-half the marital property assets in the bankruptcy estate are used in the insolvency calculation. Whether one-half or all of the marital property assets are used in this calculation is by no means clear, since the Bankruptcy Code usually treats such assets as a whole, rather than as fractional interests. *See, e.g.,* 11 U.S.C. § 541(a)(2); *see also In re Passmore*, 156 B.R. 595, 599 (Bankr. E.D. Wis. 1993).

Even if all, rather than one-half, of the marital property assets were included in measuring the entity's property, the nonmarital property of the nonfiling spouse would not be included. It is possible that if *all* of both spouses' property were included in evaluating solvency, the addition of the nondebtor's individual and predetermination date property would render the spouses solvent, thereby protecting the otherwise preferred creditor. The lack of a solvency test based on both spouses' property and obligations has been criticized, *see Pedlar, supra* § 6.76, at 386–88, but such a solvency test remains unavailable under the Bankruptcy Code.

### **(3) Fraudulent Transfers [§ 6.88]**

The trustee or debtor-in-possession is empowered to set aside certain transfers made by the debtor or debtor's spouse before filing. 11 U.S.C.

§§ 548, 544(b). A transfer subject to avoidance might have been made by the debtor to the nonfiling spouse. *See, e.g., Hinsley v. Boudloche (In re Hinsley)*, 201 F.3d 638 (5th Cir. 2000) (holding that partition agreement entered into in contemplation of divorce was fraudulent as to husband's creditors); *Browning Interests v. Allison (In re Holloway)*, 955 F.2d 1008 (5th Cir. 1992) (holding that granting to wife of security interest in debtor's assets was fraudulent as to creditors even though debtor's wife had previously made unsecured loans to debtor).

A spouse's failure to assert his or her rights in a dissolution action may result in a fraudulent transfer that is voidable by the trustee. In *Conti-Commodity Services, Inc. v. Clausen (In re Clausen)*, 44 B.R. 41 (Bankr. D. Minn. 1984), the former husband allowed his former wife to receive the family home with substantial equity by default. Citing *Britt*, 334 F.2d 896, for the proposition that a divorce decree constitutes a transfer to the extent that one party receives more than one-half of the property divided, the court found that the debtor had transferred property with the intent to hinder, delay, or defraud creditors and denied him a discharge under 11 U.S.C. § 727(a)(2)(A). *See also Corzin v. Fordu (In re Fordu)*, 201 F.3d 693 (6th Cir. 1999). *But see Harman v. Sorluccho (In re Sorluccho)*, 68 B.R. 748 (Bankr. D.N.H. 1986) (holding that marital settlement agreement fell within "reasonable range" of what court would have ordered if property division were litigated; court thus did not set aside agreement); *Grady*, 128 B.R. 462 (holding that because former spouse received only her property in divorce, there was no transfer to avoid). *See also* Steven J. Schwartz, *Marital Dissolution and Bankruptcy: The Rights of the Bankruptcy Trustee to Administer Community Property and to Avoid and to Recovery Property Divisions*, 28 Cal. Bankr. J. 523 (2006).

The trustee in *Liebzeit v. Universal Mortgage Corp. (In re Larson)*, 346 B.R. 486 (Bankr. E.D. Wis. 2006), sought to set aside the perfection of a homestead mortgage that the husband alone had granted while married. Had the mortgage perfection been set aside, the mortgage would have been preserved for the benefit of the bankruptcy estate, and loan payments made by the debtor would have inured to the benefit of unsecured creditors rather than the mortgage holder. *See* 11 U.S.C. §§ 544(a)(3), 550. The loan was a refinance, and the debtor and his nondebtor spouse were married after the debtor had taken out an initial mortgage and before the refinance. The wife did not sign the mortgage that the husband took out after the marriage, contrary to the requirement of section 706.02(1)(f). However, Wisconsin law provides that, if a

defective mortgage secures a loan that pays off a valid mortgage, equitable subrogation allows the holder of the defective mortgage to stand in the shoes of the prior valid mortgage holder. See *State Bank of Drummond v. Christophersen*, 93 Wis. 2d 148, 286 N.W.2d 547 (1980). Therefore, to the extent the prior mortgage was paid by the existing creditor, the trustee in *Larson* could not set aside the creditor's mortgage interest.

#### **(4) Lien Avoidance [§ 6.89]**

In addition to liens that may be avoided as preferences or fraudulent transfers, liens that are unsecured because the value of the property subject to the lien is less than the amount of the claim may be avoided, usually by the debtor. 11 U.S.C. § 506. The debtor may also avoid (1) nonpossessory, non-purchase money security interests in certain exempt property and (2) judicial liens on exempt property, except those that secure support debts. 11 U.S.C. § 522(f). Judicial liens securing a payment to the debtor's former spouse that arose pursuant to a divorce decree are usually not avoidable. *Farrey v. Sanderfoot*, 500 U.S. 291 (1991); *Foss v. Foss*, 200 B.R. 660 (B.A.P. 9th Cir. 1996) (holding that liens to secure payment of property division could not be avoided). However, if a judicial lien attaches to a community property asset that the debtor later acquires under a divorce decree, the debtor may still avoid the lien, provided all requirements of 11 U.S.C. § 522(f) are met. *Law Offices of Moore & Moore v. Stoneking (In re Stoneking)*, 225 B.R. 690 (B.A.P. 9th Cir. 1998); *In re Schmiedel*, 236 B.R. 393 (Bankr. E.D. Wis. 1999). Because the debtor had an interest in the asset when the lien attached and the lien impairs an exemption, it may be avoided (notwithstanding the fact that the debtor's ownership interest was later augmented to full ownership by the debtor's acquisition of the former spouse's interest in the asset, to which the lien had also attached). *Stoneking*, 225 B.R. 690; *Schmiedel*, 236 B.R. 393.

Statutory liens are not avoidable under 11 U.S.C. § 522(f). Section 49.854(2)(a) provides an example of a statutory lien for child support in Wisconsin:

If a person obligated to pay support fails to pay any court-ordered amount of support, that amount becomes a lien in favor of the department [of children and families] upon all property of the person. The lien becomes effective when the information is entered in the statewide support lien docket under

par. (b) and that docket is delivered to the register of deeds in the county where the property is located ....

The property subject to the lien is real or personal property in which the payer has a “recorded ownership interest.” Wis. Admin. Code § DCF 152.03(7).

### **g. Exemptions [§ 6.90]**

Under bankruptcy law, as under state law, a debtor is entitled to retain certain property free of the creditors’ right to collect. 11 U.S.C. § 522(d); Wis. Stat. §§ 815.18, .20, 425.106; *see also* 7 *Collier, supra* § 6.72, at 815–34. This is to allow the debtor to retain the necessities of life and the means to make a living, notwithstanding the right of creditors to satisfy their claims.

The Bankruptcy Code allows a debtor to claim either the assets described in 11 U.S.C. § 522(d) or the assets available under state law, but it allows states to prevent the use of federal bankruptcy exemptions. 11 U.S.C. § 522(b). Wisconsin has not enacted legislation to prevent use of the federal exemptions, which gives Wisconsin debtors the choice of state or federal exemptions. A debtor must use the state or federal list in its entirety and may not choose on an asset-by-asset basis. 11 U.S.C. § 522(b). Spouses filing a joint case must both choose either the state list or the federal list—one spouse may not use the state list and the other the federal list. *Id.* If a choice is available and the spouses cannot agree, they are deemed to have chosen the federal list. *Id. But see In re Hendrick*, 45 B.R. 965 (Bankr. M.D. La. 1985) (allowing nondebtor former wife to take state-law exemptions in community property).

Although all marital property assets are included in a bankruptcy estate, under federal law only “an individual debtor” may claim certain assets as exempt. 11 U.S.C. § 522(b)(1). This means that the nondebtor spouse does not have a right to remove assets from the estate as exempt. *In re DeHaan*, 275 B.R. 375 (Bankr. D. Idaho 2002); *Kapila v. Morgan (In re Morgan)*, 286 B.R. 678 (Bankr. E.D. Wis. 2002); *Burman v. Homan (In re Homan)*, 112 B.R. 356, 359–60 (B.A.P. 9th Cir. 1989) (holding that nondebtor spouse was not allowed under Fed. R. Bankr. P. 4003(a) to supplement exemptions claimed by debtor, even though list was incomplete). *See also In re Victor*, 341 B.R. 775, 781 (Bankr. D.N.M. 2006) (holding that filing spouse could claim exemption in only

her one-half interest in community property assets, even though full value of community property assets was in estate); *In re Czerneski*, 330 B.R. 240 (Bankr. E.D. Wis. 2005) (concluding that debtor did not establish “mixing” of marital property with his spouse’s individual property and was not allowed to claim exemption in her asset); David R. Knauss, Comment, *What Part of Yours Is Mine?: The Creation of a Marital Property Ownership Interest by Improving Nonmarital Property Under Wisconsin’s Marital Property Law*, 2005 Wis. L. Rev. 855. *But see Flinn v. Morris (In re Steward)*, 227 B.R. 895, 899 (B.A.P. 9th Cir. 1998) (holding that subsequent filing by other spouse and administrative consolidation of cases gave second spouse right to claim bankruptcy exemptions); *In re Crouch*, 33 B.R. 271, 274 (Bankr. E.D.N.C. 1983) (holding that exemptions must be claimed in good faith and not to defeat other spouse’s rights). Although a spouse’s state-law exemptions might keep certain 11 U.S.C. § 541(a)(2)(B) assets out of the estate (because they are only in the estate “to the extent” the assets are subject to recovery for certain claims), once marital property assets are included in the estate, the nondebtor may not claim exemptions to remove the assets from the estate. *See supra* § 6.76.

The effect on use of the federal exemptions of the debtor’s owning only a one-half interest in each item of marital property is unclear. Each exemption under 11 U.S.C. § 522(d) is for “the debtor’s interest” in each item listed. If the nondebtor may not claim his or her interest in each item of exempt property, then it would follow that these items must be sold (if nondivisible) and one-half the proceeds given to the debtor as exempt and the other half, which is the marital property interest of the nondebtor, included in the estate. 11 U.S.C. § 363(h). The nondebtor spouse’s interest in a joint-tenancy asset is not in the bankruptcy estate, in contrast to an asset classified as community property, which is in the estate in its entirety. *See supra* §§ 6.74–.77.

This rule was demonstrated in *In re Page*, 171 B.R. 349 (Bankr. W.D. Wis. 1994). In *Page*, the debtor wife attempted, pursuant to 11 U.S.C. § 522(f), to remove a garnishment lien on a check for deer damage payable to the nondebtor husband. The husband was ineligible for a discharge, having received a Chapter 7 discharge within six years before the debtor’s filing. The debtor claimed the federal exemptions under 11 U.S.C. § 522(d). The entire check was property of the estate; however, the court held that only an individual debtor could claim exemptions under 11 U.S.C. § 522(b) and (d). *Id.* at 352. Therefore, the debtor could claim only her one-half interest as exempt and could remove the



lien only from her one-half interest, not from the full amount of the check.

The court in *In re Barnes*, 14 B.R. 788, 790 (Bankr. N.D. Tex. 1981), however, took a unitary approach to the treatment of community property. The debtors were entitled to an income-tax refund, and only the wife had taxable income. The refund was due on account of excess withholding of her earned income, over which she had sole management and control. At that time, spouses could use different exemption laws, and the husband took the federal exemptions, which allowed an exemption for a tax refund, and the wife took the state exemptions, which did not. The court held that the community property tax refund was in the consolidated estate, and either spouse could claim an exemption in the entire amount, regardless of which spouse earned it. The court disagreed with *In re Smith*, 5 B.R. 227 (Bankr. S.D. Ohio 1980), not a community property case, in which the court in a joint case allowed exemption by only one spouse of the “debtor’s interest” in a tax refund earned by only that spouse.

Under Wisconsin law, the debtor’s interest in each item listed is exempt, but the debtor’s spouse is also entitled to an exemption from execution for his or her interest in the item, and with the exception of income, the spouses’ exemptions may be combined to claim a single asset as exempt. Wis. Stat. § 815.18(8); *Bank One, Appleton, NA*, 176 Wis. 2d at 223. Arguably, the grant of state exemptions under 11 U.S.C. § 522(b) incorporates the state’s grant to both spouses of the right to retain exempt assets. This interpretation is in keeping with the policy of preserving assets for the debtor to maintain the necessities of life and the means to make a living. Wis. Stat. § 815.18(1); see 3 *Collier, supra* § 6.72, ¶ 522.02. The ruling in *Page*, discussed above, is not inconsistent with this interpretation, as the asset in question in that case was not exempt under Wisconsin law.

The alternative available under 11 U.S.C. § 522(b)(3)(A) refers to claiming “any property,” rather than the debtor’s interest in property, exempt under the state exemptions or under federal exemptions other than 11 U.S.C. § 522(d) (i.e., under the federal nonbankruptcy exemptions). Debtors claiming assets eligible for an exemption under state law must refer to the particular Wisconsin statute being applied to determine if it is the asset or the debtor’s interest in the asset that is exempt. See, e.g., Wis. Stat. §§ 425.106(1), 815.18(3), .20; see also 7 *Collier, supra* § 6.72, at 815–34 (federal nonbankruptcy exemptions).

On the other hand, for the debtor choosing the alternative available under 11 U.S.C. § 522(b)(1), the federal exemptions under 11 U.S.C. § 522(d) allow exemption of only “the debtor’s interest” in the list of assets.

The Wisconsin homestead-exemption statute, section 815.20, allows an exemption for a homestead occupied and owned in whole or in part by a debtor. The statute states that the exemption may be claimed for a homestead owned by a husband and wife jointly, in common, or as marital property. Therefore, for a debtor claiming the Wisconsin exemptions, it appears that the protection extends to the entire homestead, not merely the debtor’s fractional interest.

A debtor may claim only property of the estate as exempt. 11 U.S.C. § 522(b). If one spouse files a bankruptcy petition, which brings all marital property into his or her bankruptcy estate under 11 U.S.C. § 541(a)(2), and the other spouse subsequently files, property that may not be claimed by the nondebtor spouse is liquidated in the first estate. Thus, the asset is not in the estate of the second spouse and may not be claimed. However, if spouses file a joint petition, assets classified as marital property are in both estates. *Ageton v. Cervenka (In re Ageton)*, 14 B.R. 833 (B.A.P. 9th Cir. 1981); *In re Barnes*, 14 B.R. 788 (Bankr. N.D. Tex. 1981). Substantive consolidation may be appropriate under such circumstances, especially as to the marital property assets in both bankruptcy estates. *Ageton*, 14 B.R. 833; *Barnes*, 14 B.R. 788; see 2 *Collier, supra* § 6.72, ¶ 302.05; see also Fed. R. Bankr. P. 1015, 2009.

If the same property is in subsequent estates, which occurs if one spouse files a bankruptcy petition and claims an exemption in a marital property asset and the other spouse later files, an exemption may be claimed again in the same asset. In *Texaco, Inc. v. Bartlett (In re Bartlett)*, 24 B.R. 605, 608 (B.A.P. 9th Cir. 1982), which arose under the California community property system, the entire homestead was claimed as exempt in each spouse’s bankruptcy. The debtor claimed state (California) exemptions, and her husband in a previous case had claimed the same assets under the federal exemptions. The court held that a debtor is not limited to one exemption of his or her interest in a community property asset; debtors and their spouses may claim the asset as many times as necessary to preserve the exemption.

The Wisconsin statute allowing an exemption for tools and equipment used by a debtor in earning a living applies to property used “in the business of the debtor or the business of a dependent of the debtor.”

Wis. Stat. § 815.18(3)(b). For the purpose of claiming exemptions, the term *dependent* is defined to include the debtor's spouse, regardless of whether the spouse is actually dependent. 11 U.S.C. § 522(a)(1); *cf.* Wis. Stat. § 815.18(2)(d) (“‘Dependent’ means any individual, including a spouse, who requires and is actually receiving substantial support and maintenance from the debtor.”). A bankruptcy court, interpreting the analogous New Mexico exemption statute, disallowed the exemption claimed by one joint debtor spouse for tools of a business in which only the other joint debtor was active, even though the tools were community property. *In re Bryan*, 126 B.R. 108 (Bankr. D.N.M. 1991). The court reasoned that the spouse had no business and could not claim such an exemption. The New Mexico statute did not apply to the business of a dependent of the debtor as does section 815.18(3)(b). Even though the Wisconsin definition of dependent provides that the dependent must be actually receiving support, the definition under 11 U.S.C. § 522(a)(1) does not, and the bankruptcy definition applies whether the debtor is claiming state or federal exemptions under 11 U.S.C. § 522(b). Consequently, a Wisconsin debtor should be able to claim an exemption in assets used solely in the business of the other spouse.

## 2. Involuntary Petitions [§ 6.91]

Section 303 of the Bankruptcy Code deals with involuntary bankruptcy petitions filed by creditors. The creditors qualified to initiate such petitions are limited to those having claims against the person (as opposed to claims against the property of a spouse who is not the obligated spouse). 11 U.S.C. § 303(b). The debtor must be the incurring spouse to be personally liable, unless the debtor is the obligated spouse under the necessities doctrine. *See supra* §§ 6.4–6. A creditor having a claim only against the debtor's property, such as a creditor entitled to reach marital property assets to satisfy a family-purpose obligation incurred by a spouse under the family-purpose doctrine, Wis. Stat. § 766.55(2)(b), is not qualified to file an involuntary petition for the bankruptcy of the nonincurring spouse. *See* 11 U.S.C. § 303.

The test for granting an involuntary petition is whether “the debtor is generally not paying such debtor's debts as such debts become due.” 11 U.S.C. § 303(h)(1). The “debtor's debts” do not include obligations incurred by the debtor's spouse. *In re Karber*, 25 B.R. 9, 13 (Bankr. N.D. Tex. 1982). Therefore, creditors as to obligations incurred by a debtor's spouse may not initiate a petition for involuntary bankruptcy of

the nonobligated spouse. *See King v. Fidelity Nat'l Bank*, 712 F.2d 188, 190 (5th Cir. 1983); *Karber*, 25 B.R. at 13; *see also In re Gale*, 177 B.R. 531 (Bankr. E.D. Mich. 1995); *In re Jones*, 112 B.R. 770 (Bankr. E.D. Va. 1990); 2 *Collier*, *supra* § 6.72, ¶ 303.07; *Pedlar*, *supra* § 6.76, at 354–57. Furthermore, one spouse may not force the other to involuntarily join in a joint petition. *In re McDonald*, No. Civ. A. 93-4176, 1994 WL 160484 (E.D. La. Apr. 22, 1994).

### 3. Claims Against Debtor and Debtor's Spouse [§ 6.92]

#### a. In General [§ 6.93]

All claims sought to be discharged by a debtor must be included in the bankruptcy schedules, and the creditors listed must be notified that the bankruptcy petition has been filed. 11 U.S.C. § 523(a)(3). All creditors, including those having community claims, *see infra* §§ 6.95–.104, are entitled to notice. 11 U.S.C. § 342(a). Since it appears that marital property assets are part of the bankruptcy estate regardless of who has possession of them or how they are held, *see supra* §§ 6.74–.77, any creditor having a claim against the nondebtor spouse should file a claim in the bankruptcy estate of the debtor spouse who did not incur the debt. This filing is necessary to reach marital property assets that would have been available to the creditor of the nondebtor spouse if the bankruptcy had not been filed. Also, under some circumstances, creditors of the nondebtor spouse may be entitled to distributions of the debtor's individual property that would not be available under state law. *See infra* § 6.105. It is particularly important that creditors keep records of the names and addresses of, and possibly other identifying information relating to, debtors' spouses to ensure that claims can be filed in such cases.

➤ **Note.** Claims between former spouses arising in a dissolution decree, which must be addressed in the bankruptcy of a former spouse who is obligated by the decree, are beyond the scope of this chapter. However, under certain circumstances, these obligations may relate to the former ownership of community property. *See, e.g., Smith v. Smith (In re Smith)*, 229 B.R. 792 (Bankr. E.D. Cal. 1998) (holding that obligation to pay former spouse or debtor her share of community

property divided by divorce decree was excepted from discharge under 11 U.S.C. § 523(a)(15)).

### **b. Claims Against Debtor or Debtor's Property** **[§ 6.94]**

In general, a claim is any right to payment. 11 U.S.C. § 101(5). Section 102(2) of the Bankruptcy Code defines the term claim against the debtor to include a claim against the debtor's property. It appears from the literal language of that section that an obligation that may be satisfied from marital property in which the debtor has an interest constitutes a claim against the debtor. Creditors having a right to recover property of the debtor because those rights arose before the pre-petition death of the debtor's spouse or before the pre-petition dissolution of the debtor's marriage would also have claims against property of the debtor. *See supra* §§ 6.44–.47.

➤ **Note.** Although the legislative history of 11 U.S.C. § 102(2) indicates the statute was intended to apply only to nonrecourse mortgages for which the debtor was not personally liable, the U.S. Supreme Court in *Johnson v. Home State Bank*, 501 U.S. 78 (1991), held the section applicable in that case, which involved a mortgage on the debtor's real estate for which the debtor was not personally liable. The literal language clearly made the application of 11 U.S.C. § 102(2) appropriate, and the mortgage was held to be a claim.

All obligations for which the debtor is personally liable constitute claims against the debtor. A family-purpose obligation incurred by the nondebtor spouse, which under section 766.55(2)(b) may be satisfied from all marital property assets, is likewise a claim under the Bankruptcy Code because it is a claim against property of the debtor. 11 U.S.C. § 102(2). Other obligations described in section 766.55(2)(c)–(d) may or may not be claims against the debtor or the debtor's property, depending on the nature of the obligation and the classification of property in the estate. For example, tort and nonfamily-purpose obligations of the nonfiling spouse are collectible only from the nonfiling spouse's nonmarital property assets and from the nonfiling spouse's share of marital property—not from the debtor's property. If there are marital property assets in the bankruptcy estate that are available to satisfy the category of debt under section 766.55(2)(c)–(d) (such as accumulation of

the debtor's marital property wages, which are available to satisfy a premarriage obligation of the debtor), then the creditor has a claim. This distinction is probably not crucial, however, because a creditor's having a community claim, which is used to determine the distribution of assets, turns on the ability to satisfy the obligation from hypothetical assets of a particular classification, not actual assets. *See infra* §§ 6.95–.104.

In a bankruptcy proceeding, the issue of whether a creditor's right to payment constitutes a claim against the debtor is relevant under certain circumstances that are not related to payment, such as in determining insolvency for the purpose of avoiding preferences. *See supra* §§ 6.85–.89.

### **c. Community Claims [§ 6.95]**

#### **(1) In General [§ 6.96]**

Another important definition affecting the rights of creditors in a bankruptcy case is the definition of the term community claim. 11 U.S.C. § 101(7). Whether a claim is a community claim affects which sub-estates under 11 U.S.C. § 726(c) are used to pay the claim. *See infra* § 6.105. It also determines whether the discharge injunction under 11 U.S.C. § 524(a)(3) prevents recovery by the creditor of marital property assets acquired after the discharge. *See infra* §§ 6.106–.110. The total amount of community claims is also used to determine a debtor's eligibility for filing a Chapter 13 case under 11 U.S.C. § 109(e), whether or not the debtor is personally liable for the debts in question. *In re Monroe*, 282 B.R. 219 (Bankr. D. Ariz. 2002). Analysis of the various types of obligations under section 766.55 is necessary to see if they meet the definition of community claim. *See also supra* §§ 6.74–.77, *infra* § 6.105.

A community claim is a claim that arose before the commencement of the bankruptcy case and for which property described in 11 U.S.C. § 541(a)(2) (community property that is property of the estate, *see supra* §§ 6.74–.77), is liable, “whether or not there is any such property at the time of the commencement of the case.” 11 U.S.C. § 101(7). Therefore, no reference need be made to the actual classification of property in the estate to determine a creditor's status. If it is hypothetically possible for the estate to hold marital property assets described in 11 U.S.C. § 541(a)(2) that would be available to satisfy the creditor's claim, then

the creditor qualifies as having a community claim. There are no provisions under 11 U.S.C. § 101(7) for different classes of community claims; therefore, if a creditor achieves that status, the creditor will be treated for distribution purposes in the same manner as other community creditors in the same class. See 2 *Collier, supra* § 6.72, ¶ 101.07; *FDIC v. Soderling (In re Soderling)*, 998 F.2d 730 (9th Cir. 1993) (holding that restitution for federal crime may be satisfied from community property under California law and thus is community claim); *Grimm v. Grimm*, 82 B.R. 989, 991–93 (Bankr. W.D. Wis. 1988). But see *infra* § 6.104 (disallowance of some claims).

It appears that *all* categories of obligations under section 766.55(2), whether incurred by the debtor spouse or the nondebtor spouse, meet the definition of community claim under 11 U.S.C. § 101(7) for the reasons set forth in sections 6.97–.104, *infra*.

See also *Arcadia Farms Ltd. v. Rollinson (In re Rollinson)*, 322 B.R. 879 (Bankr. D. Ariz. 2005) (holding that note signed by both spouses in favor of wife's employer as reimbursement for wife's embezzlement was community claim).

Claims are determined as of the filing of the case, notwithstanding that they might be paid well after filing. Thus, the court in *In re Nelson*, 308 B.R. 343 (Bankr. E.D. Wis. 2004), held that claims allowed in a debtor-husband's Chapter 13 case could continue to be paid through the plan, even though after the case was filed, the debtor-wife converted her case to Chapter 7 and received her discharge. The wife's Chapter 7 discharge would prevent recovery of community property under 11 U.S.C. § 524(a)(3), and community property wages funded the husband's Chapter 13 plan; however, the allowance of claims in the husband's case took place before the Chapter 7 discharge, and the wife's subsequent discharge had no effect.

## **(2) Support Obligations [§ 6.97]**

An obligation for support, which one spouse can recover from the other, may be satisfied from all marital property assets and from all other assets of the obligated spouse. Wis. Stat. § 766.55(2)(a). Since the assets recoverable by one spouse having a support claim against the other are assets described in 11 U.S.C. § 541(a)(2), a support obligation of either spouse qualifies as a community claim.

### (3) Obligations Incurred in Interest of Marriage or Family [§ 6.98]

Family-purpose obligations may be satisfied from all marital property assets and from all other property of the incurring spouse. Wis. Stat. § 766.55(2)(b); *see supra* §§ 6.7–.22. It is immaterial whether a family-purpose obligation is incurred by the debtor or the debtor’s spouse or whether the debtor or the debtor’s spouse is obligated under the necessities doctrine; in any of these situations, the family-purpose obligation may be satisfied from property described in 11 U.S.C. § 541(a)(2)(A) and (B). Therefore, a family-purpose obligation incurred by either spouse is a community claim.

➤ **Comment.** The presumption that all obligations are incurred in the interest of the marriage or the family places most claims in this category. *See* Wis. Stat. § 766.55(1).

### (4) Premarriage Obligations [§ 6.99]

An obligation, including a tort, incurred by the debtor before marriage, or one attributable to an obligation of the debtor that arose before marriage, may be satisfied from the debtor’s nonmarital property assets and from marital property assets that would have been available if the marriage had not taken place. Wis. Stat. § 766.55(2)(c)1.; *see supra* § 6.24. Earnings of a married debtor are an example of a type of marital property asset available to the debtor’s premarriage creditor. Such funds are marital property described in 11 U.S.C. § 541(a)(2). Therefore, a debtor’s premarriage obligation is a community claim. 11 U.S.C. § 101(7). It is immaterial whether the estate contains such property. *Id.*

A premarriage obligation of the nondebtor spouse may be satisfied from marital property assets that would have belonged to the nondebtor if the marriage had not taken place. Wis. Stat. § 766.55(2)(c)1. Such marital property assets include, for example, the accumulation of earned income of the nondebtor. If they exist, these earnings are includible in the bankruptcy estate because they are “liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor’s spouse, to the extent that such interest is so liable.” 11 U.S.C. § 541(a)(2)(B); *see supra* § 6.76. Since the designation of a claim as a community claim is made without



reference to the actual classification of property in an estate, it is only necessary that the estate can theoretically hold such property. Consequently, the premarriage creditor of the nondebtor spouse has a community claim in the debtor spouse's bankruptcy estate, whether the estate actually includes an asset that would have been the nondebtor spouse's property but for the marriage. *See, e.g., In re Pfalzgraf*, 236 B.R. 390 (Bankr. E.D. Wis. 1999) (holding that nondebtor spouse's former spouse had community claim for child-support arrearage in debtor's Chapter 13 case).

### **(5) Obligations Arising Before January 1, 1986 [§ 6.100]**

An obligation incurred by a debtor spouse before January 1, 1986, or an obligation attributable to an obligation arising before January 1, 1986, may be satisfied from the debtor's nonmarital property assets and from marital property assets that would have been available but for enactment of the Act. Wis. Stat. § 766.55(2)(c)2.; *see supra* § 6.25. The obligation may therefore be satisfied from marital property described in 11 U.S.C. § 541(a)(2).

The pre-January 1, 1986, obligations of the nondebtor spouse are also community claims for the same reasons that the nondebtor's premarriage obligations are community claims. *See supra* § 6.99; *In re Pfalzgraf*, 236 B.R. 390 (Bankr. E.D. Wis. 1999).

### **(6) Tort Obligations [§ 6.101]**

Tort obligations of the debtor spouse that are incurred during marriage may be satisfied from the debtor's nonmarital property assets and from the debtor's one-half interest in marital property assets. Wis. Stat. § 766.55(2)(cm); *see supra* §§ 6.26–.28. No order of satisfaction is required. Since marital property assets described in 11 U.S.C. § 541(a)(2) include the debtor's one-half interest in those assets, the debtor's tort obligation is a community claim. 11 U.S.C. § 101(7). *See also In re Silver*, 367 B.R. 795 (Bankr. D.N.M. 2007), *aff'd*, 378 B.R. 418 (B.A.P. 10th Cir. 2007) (holding that tort-judgment creditor of debtor's husband, for judgment obtained before divorce, had standing as community creditor to move to revoke discharge).

Marital property assets included in the estate under 11 U.S.C. § 541(a)(2) also include the nondebtor spouse's one-half interest in such assets. These marital property assets are available under the Act to satisfy the tort obligations of the nondebtor spouse. Wis. Stat. § 766.55(2)(cm); *see supra* §§ 6.26–.28. Therefore, a tort obligation of the nondebtor spouse is also a community claim. 11 U.S.C. § 101(7).

Premarriage and pre-effective date tort obligations are considered premarriage and pre-effective date obligations. *See supra* §§ 6.99, .100. Tort obligations arising while the spouses are married and after January 1, 1986, but before both spouses live in Wisconsin fall into the category of obligations recoverable without reference to the Act. *See infra* § 6.103, *supra* § 6.30.

### **(7) Other Obligations [§ 6.102]**

Obligations incurred by the debtor during marriage that are not incurred in the interest of the marriage or the family may be satisfied first from nonmarital property assets of the debtor and then from the debtor's one-half interest in marital property assets, in that order. Wis. Stat. §§ 766.55(2)(d), .01(8); *see supra* §§ 6.26–.28. The estate may include the debtor's interest in the marital property assets subject to recovery for an “other” claim under section 766.55(2)(d), which qualifies the obligation as a community claim. 11 U.S.C. § 101(7).

The nondebtor spouse's other obligations may be satisfied first from the nondebtor's nonmarital property assets and then from the nondebtor's one-half interest in marital property assets, in that order. Wis. Stat. §§ 766.55(2)(d), .01(8); *see supra* §§ 6.26–.28. The nondebtor's interest in marital property assets available under section 766.55(2)(d) is property described in 11 U.S.C. § 541(a)(2); consequently, the other obligations of the nondebtor spouse are community claims. *See Phillips v. Phillips (In re Phillips)*, 175 B.R. 901 (Bankr. E.D. Tex. 1994) (holding that debtor's former wife's claims for pre-petition misconduct were community claims).

## (8) Obligations Not Provided for Under Act [§ 6.103]

The definition of the term during marriage refers to the period during which both spouses reside in Wisconsin that begins on the determination date and ends at dissolution or the death of a spouse. Wis. Stat. § 766.01(8). Obligations incurred while spouses are married and after January 1, 1986, but before the spouses move to Wisconsin are not incurred during marriage. *See id.* Similarly, obligations incurred after a spouse no longer resides in Wisconsin are not incurred during marriage. *See id.* Therefore, such obligations incurred by either spouse do not fit any of the categories under section 766.55(2). Presumably, such obligations are recoverable without reference to the Act. The creditor could recover assets based on the personal liability of the spouse under the common law system of ownership. Assets classified as marital property, such as the wages of the incurring spouse, could be recovered to satisfy such obligations. These obligations may therefore be satisfied from property described in 11 U.S.C. § 541(a)(2), and so they would be community claims.

An example of how such an obligation might become an issue in the bankruptcy context arose in *In re Sweitzer*, 111 B.R. 792 (Bankr. W.D. Wis. 1990) (citing 3 Keith A. Christiansen et al., *Marital Property Law in Wisconsin* § 13.10c, at 13-23, 13-24 (State Bar of Wisconsin ATS-CLE 2d ed. 1986 & Supp. 1988)). In that case, only the wife was a bankruptcy debtor. In 1988, while the spouses were married and both were residents of Ohio, judgment on a bank debt was entered against the husband alone. After the spouses moved to Wisconsin, the wife filed her petition under Chapter 7 and received her discharge. The Ohio creditor then attempted to garnish the husband's wages in execution on the judgment against him. The debtor and her husband contended that the injunction under 11 U.S.C. § 524(a)(3) prevented recovery from after-acquired marital property, including the husband's wages. *See infra* § 6.108.

The discharge injunction applies only to community claims, *see* 11 U.S.C. § 524(a)(3), and the *Sweitzer* court rejected the spouses' assertion that the obligation was a community claim as defined by 11 U.S.C. § 101. The court reasoned that under conflict-of-laws principles, Ohio law controlled the obligation. Since Ohio is not a community property state, for purposes of this action the husband's wages were not

community property, and hence there was no community claim. *Sweitzer*, 111 B.R. at 795.

Such a result is inconsistent with the language of 11 U.S.C. § 101(7) and the holding of *Pacific Gamble Robinson Co. v. Lapp*, 622 P.2d 850 (Wash. 1980), which the *Sweitzer* court cited to support its conclusion. Another state's (e.g., Ohio's) law might determine the enforceability of the judgment and prescribe the universe of property available for recovery (a result consistent with section 766.55(3)), but it cannot change the classification of that property. As the court noted in *Pacific Gamble Robinson*:

[A] fair application of Colorado law to [a] debt in an action brought in Washington is that the same property subject to payment of a debt in Colorado, including . . . wages and acquisitions, is likewise subject to payment of the debt in Washington, *notwithstanding such property is characterized as "community" under Washington law.*

*Id.* at 857 (emphasis added). In *Sweitzer*, the spouses' determination date had occurred before the wife's bankruptcy petition was filed, and the property in question (the husband's wages) constituted marital property funds and hence community property described in 11 U.S.C. § 541(a)(2). Under 11 U.S.C. § 101(7), a community claim is a claim for which "property of the kind specified in § 541(a)(2) of this title is liable, whether or not there is any such property at the time of the commencement of the case." Since community property described in 11 U.S.C. § 541(a)(2) was available for recovery by the creditor in *Sweitzer* when Ohio law was applied, the definition of community claim applied, and it appears that the injunction should have been applied to prevent recovery of after-acquired marital property of the debtor and her husband.

The *Sweitzer* court chose to apply section 766.55(3) in determining what property would have been available for satisfaction of the obligation if the bankruptcy had not intervened and recovery had been attempted in Wisconsin. Since the debt did not arise during marriage, the Act did not apply, and the assets available to the creditor had the bankruptcy not occurred would be the same. However, the obligation is still a community claim. *See also In re Porter*, No. C-92-4089 FMS, 1993 WL 106884 (N.D. Cal. Apr. 5, 1993) (holding that IRS claim was community claim, even though it was separate debt under California law,

because it could be satisfied only from debtor's share of community property).

There might be circumstances in which an obligation might not be a community claim if the jurisdiction in which the obligation was incurred was a community property state and the laws of that jurisdiction prohibited recovery from community property. *See Merlino v. Weinstein (In re Merlino)*, 62 B.R. 836 (Bankr. W.D. Wash. 1986) (discussed in section 6.104, *infra*).

### **(9) Disallowance or Partial Disallowance of Certain Community Claims [§ 6.104]**

It appears that a claim on a nonfamily-purpose obligation incurred by the nondebtor spouse could be disallowed if the nondebtor spouse has sufficient nonmarital property assets to satisfy the claim. Section 502(b)(1) of the Bankruptcy Code states that a claim may be disallowed if it is unenforceable against the debtor or the debtor's property under any applicable law. The fact that the individual property assets and predetermination date property assets of the incurring spouse must be applied to the obligation before marital property assets may be reached should be sufficient for disallowance, as long as the nondebtor spouse has sufficient individual property assets and predetermination date property assets to satisfy the claim. If these nonmarital assets of the nondebtor spouse are sufficient for satisfaction, there would be no assets in the estate from which the creditor could recover.

If a creditor having such a claim against the nondebtor spouse has unsuccessfully attempted to collect from nonmarital property, the creditor may wish to allege this in its claim. However, because of the time limit for filing claims (90 days after the first date set for the meeting of creditors, Fed. R. Bankr. P. 3002(c)), the creditor should file a claim whether or not collection from the nondebtor's nonmarital property assets has been attempted. It might be possible to attempt recovery from the nondebtor's nonmarital property assets after the claim is filed but before distributions are made. Conversely, the debtor or other party in interest may object to a claim if the creditor has not attempted recovery from the nonmarital assets of the nondebtor spouse.

A claim to which the Act does not apply may be disallowed for reasons applicable to the jurisdiction in which it was incurred. *See* 11

U.S.C. § 502(b)(1); *see, e.g., Merlino v. Weinstein (In re Merlino)*, 62 B.R. 836 (Bankr. W.D. Wash. 1986) (applying Washington law to disallow separate creditor's claim when estate included only community property).

The debtor in that case had incurred a separate debt under Washington law, and as a result only his separate property was subject to recovery by the creditor. Since community property could not be used to satisfy the debt, the creditor had a noncommunity rather than a community claim. Noncommunity claims were payable only out of sub-estate C (nonmarital property and other property) and not any other sub-estate. Since the debtor had only community property—which could be used to pay creditors under sub-estates A, B, and D, but not sub-estate C—the creditor could recover nothing from the bankruptcy estate. A court reached a similar result in applying Idaho law in *In re Hicks*, 300 B.R. 372 (Bankr. D. Idaho 2003).

A claim on a nonfamily-purpose obligation incurred by the nondebtor spouse can be partly a community claim and partly a noncommunity claim, much in the same way that an undersecured creditor can have a claim that is partly secured and partly unsecured. *See* 11 U.S.C. § 506. To the extent that the nondebtor spouse has nonmarital property available for satisfaction, the claim should be disallowed. Similarly, a claim could be allowed in part and disallowed in part based on the classification of property in the estate itself. *See Merlino*, 62 B.R. 836 (holding that under Washington law, creditor could recover only separate property, and only community property was in bankruptcy estate; thus, classification of actual estate assets can result in disallowance of claim).

➤ **Example.** Assume that a debtor's bankruptcy estate has \$5,000 in marital property assets generated by the debtor spouse and \$2,000 in marital property assets generated by the nondebtor spouse. One of the nondebtor spouse's nonfamily-purpose creditors is owed \$20,000. The nondebtor spouse has no nonmarital property. Only the \$2,000 of the marital property assets generated by the nondebtor would be subject to recovery under Wisconsin law, Wis. Stat. § 766.55(2)(d), and the remaining amount of the claim would be disallowed, since 11 U.S.C. § 502(b)(1) provides that a claim will be disallowed to the extent it is unenforceable against the debtor or property of the debtor under any applicable law. The creditor's \$2,000 claim would share pro rata with other community claims.

In addition, it might be that a claim on a nonfamily-purpose obligation incurred by the debtor spouse can be partly a community claim and partly a noncommunity claim. It is not clear from 11 U.S.C. § 101(7) whether the definition of community claim is satisfied only if *both* spouses' interests in hypothetical community property assets are recoverable or whether it is sufficient if only the *debtor's* interest is recoverable. Tort obligations, for example, may be satisfied only from the tortfeasor spouse's nonmarital property and from the tortfeasor spouse's interest in marital property. Wis. Stat. § 766.55(2)(cm). It is arguable that a tort obligation does not give rise to a community claim because the creditor may not recover both spouses' interests in any type of marital property asset. *But see In re Porter*, No. C-92-4089 FMS, 1993 WL 106884 (N.D. Cal. Apr. 5, 1993) (holding that separate debt for postseparation taxes was community claim and allowing tax lien on debtor's one half of proceeds of sale of community property house). Alternatively, it is arguable that even if only one half of a marital property asset is recoverable for a tort claim, this is sufficient to meet the definition of community claim. If the latter interpretation were correct, it might be necessary to allow the claim in part and disallow the claim in part. Since 11 U.S.C. § 502(b)(1) provides that a claim will be disallowed to the extent it is unenforceable against the debtor or property of the debtor under any applicable law, the tort creditor's claim might be disallowed to the extent it would be necessary to pay that claim from the nontortfeasor's marital property interest in the estate. A claim for an obligation under section 766.55(2)(d) or for a predetermination date obligation might similarly require disallowance of a portion of the claim if allowance would result in payment from the nonobligated spouse's interest either in marital property assets or in nonmarital property assets in the estate. This issue could arise in a case in which one spouse filed, or it could arise in a joint case when claims against one spouse would be disallowed if it is necessary to distribute the other spouse's interest in marital property assets.

If a portion of a community claim is disallowed because of how the estate's assets are classified, it might be necessary to invoke the doctrine of marshaling assets, requiring the trustee to pay, for example, a tort creditor from assets attributable to the debtor and to pay other community claimants from marital assets attributable to the nondebtor spouse. The standards applicable in Wisconsin to the doctrine of marshaling of assets are found in *Moser Paper Co. v. North Shore Publishing Co.*, 83 Wis.2d 852, 860, 266 N.W.2d 411 (1978). This

result appears to be incompatible with the distribution scheme of 11 U.S.C. § 726(c). *See infra* § 6.105.

#### **4. Administration of Bankruptcy Estate; Payment of Claims [§ 6.105]**

The bankruptcy estate is administered by a trustee or by a debtor-in-possession having the powers of a trustee. *See* 11 U.S.C. §§ 704, 1106, 1107, 1202, 1302. Among other things, the trustee is responsible for converting the estate to cash, paying expenses, and making distributions to creditors, all under the jurisdiction of the bankruptcy court. *See* 11 U.S.C. §§ 704, 1106, 1107, 1202, 1302. The bankruptcy estate includes both nonmarital property of the debtor and marital property of both spouses, *see supra* §§ 6.74–77; claims may include all the categories of obligations of either or both of the spouses listed under section 766.55(2), *see supra* §§ 6.92–104. Since all marital property assets are in both spouses' estates if both are debtors, it is a practical necessity that the estates be consolidated for administration. *Ageton*, 14 B.R. at 835–36; *In re Knobel*, 167 B.R. 436 (Bankr. W.D. Tex. 1994). *But see Hicks*, 300 B.R. 372 (holding that joint debtors' estates had to be administered separately because wife's estate had separate property that was not recoverable under Idaho law for certain claims against husband; community property was in both estates).

When community property is included in the estate, the trustee, after paying administrative expenses, pays various types of claims in the following order and manner:

1. *Sub-estate A—marital property.* First, community claims against the debtor or the debtor's spouse are paid from marital property, except to the extent that such property is solely liable for the debts of the debtor and not his or her spouse. 11 U.S.C. § 726(c)(2)(A).

➤ **Comment.** The exception refers to states using the managerial system of incurring obligations, *see supra* § 5.11, and does not apply in Wisconsin, since all marital property is included in this sub-estate.

2. *Sub-estate B—not applicable.* Second, to the extent that community claims against the debtor are not paid from the first sub-estate, such



community claims are paid from community property that is solely liable for the debtor's debts. 11 U.S.C. § 726(c)(2)(B).

➤ **Comment.** This sub-estate does not apply in Wisconsin, since there is no such category under section 766.55(2).

3. *Sub-estate C—nonmarital property and other property.* Third, to the extent that all claims against the debtor, including community claims against the debtor, are not paid from the previous two sub-estates, such claims are paid from other property available only for the debts of the debtor (i.e., individual and predetermination date property). 11 U.S.C. § 726(c)(2)(C).

➤ **Comment.** Property in this sub-estate also includes inheritances, marital settlements, and life insurance proceeds to which the debtor becomes entitled within 180 days of filing and any voidable transfers made by the debtor or the debtor's spouse, such as fraudulent conveyances or preferences recovered by the trustee. *See supra* §§ 6.85–.89.

4. *Sub-estate D—any remaining property.* Fourth, to the extent that community claims against the debtor or the debtor's spouse are not paid from the previous sub-estates, such claims are paid from all remaining property of the estate. 11 U.S.C. § 726(c)(2)(D).

Claims of creditors are paid from the property of the sub-estates, in order, beginning with all claims qualifying under 11 U.S.C. § 726(c)(2)(A) and exhausting all property in that sub-estate, and then proceeding through the sub-estates in 11 U.S.C. § 726(c)(2)(B), (C), and (D). Within the sub-estates, claims are paid according to priorities set forth in 11 U.S.C. § 507. 11 U.S.C. § 726(a). Certain claims may qualify under more than one sub-estate. For example, an obligation incurred by a debtor may be paid from sub-estate A (marital property) and then, to the extent the obligation is not satisfied, from sub-estate C (nonmarital property). A creditor having an obligation incurred by the debtor's spouse may also receive a pro rata share of sub-estate A, but a creditor in this case would have no right to recover from sub-estate C. However, if the debtor's individual property in sub-estate C exceeds the amount necessary to pay all the debtor's personal obligations, any funds remaining in sub-estate A, B, or C would fall into sub-estate D and would then be available to pay the claims incurred by the debtor's

spouse. It appears in this instance that the nonmarital property of one spouse may be used to satisfy community claims incurred by the other spouse, a result that would not occur under section 766.55(2) (unless the obligation is for necessities). *See supra* §§ 6.2–.31.

The Bankruptcy Code provides no procedure for classifying assets for placement in the various sub-estates, but the trustee or debtor-in-possession probably could obtain bankruptcy court approval of a proposed classification of assets following notice to all creditors, since their rights may be affected by the classification. 6 *Collier, supra* § 6.72, ¶ 726.05. It may also be necessary to identify sub-estates in Chapter 11 and Chapter 13 proceedings to determine whether proposed payment plans result in creditors' receiving less than they would under a Chapter 7 bankruptcy. Since all obligations of the debtor and the debtor's spouse are classified as community claims (subject to possible disallowance, *see supra* § 6.104), and all of both spouses' property is presumed to be marital property, Wis. Stat. § 766.31(2), such classification would not be necessary in most cases. It is necessary to classify property in more complicated estates containing both marital and nonmarital property and in situations in which claims are filed for obligations incurred by both spouses.

Administrative expenses are paid from property of the estate "as the interest of justice requires." 11 U.S.C. § 726(c)(1); *see also* Pedlar, *supra* § 6.76, at 370. If administrative expenses are incurred in connection with the administration of a particular sub-estate, that sub-estate is charged with the expenses. General expenses for overall administration would usually be equitably prorated among the sub-estates having assets, since this would be equitable in most cases. Pedlar, *supra* § 6.76, at 370.

As was previously noted, the categories of obligations under section 766.55(2) do not precisely fit the sub-estate categories designated in 11 U.S.C. § 726(c). Nevertheless, the federal bankruptcy rules for determining distribution to creditors supersede the state-law rules of debt satisfaction. *See* 6 *Collier, supra* § 6.72, ¶ 541.15. Simply stated, the effect appears to be that since all types of obligations under section 766.55(2) may be satisfied from all or part of marital property that could hypothetically be owned by spouses, any obligation of either the debtor or the debtor's spouse within section 766.55(2) is a community claim under 11 U.S.C. § 101(7). All creditors having community claims share pro rata in available marital property under sub-estate A. Unless part of

a claim is disallowed, *see supra* § 6.104, this pro rata sharing gives a distinct advantage to certain creditors, such as a tort creditor of either spouse who under the Wisconsin Marital Property Act may reach only the tortfeasor spouse's one-half interest in marital property. Wis. Stat. § 766.55(2)(cm); *see also* Pedlar, *supra* § 6.76, at 363.

Recoveries of preferential transfers under 11 U.S.C. § 547 and other voidable transfers, *see supra* §§ 6.85–.89, are included in sub-estate C. Such recoveries are included in this category because they are property “other than property of the kind specified in section 541(a)(2) of this title.” 11 U.S.C. § 726(c)(2)(C). These are transfers of any property by the debtor or transfers of marital property by the debtor's spouse, if the transfers were subject to avoidance by the trustee.

➤ **Comment.** The placement of the recoveries discussed above in sub-estate C—the sub-estate available to pay only the debts of the debtor and not those of the debtor's spouse—has been criticized. *See* Pedlar, *supra* § 6.76, at 372. Logically, it seems that these recoveries should be in the sub-estate to which the property would have belonged had the voided transfer never occurred, but this does not appear to be the case.

## **5. Discharge [§ 6.106]**

### **a. Effect on Marital Property Acquired After Filing [§ 6.107]**

#### **(1) During Marriage [§ 6.108]**

In many, if not most, instances, a married debtor under the Wisconsin Marital Property Act who files for bankruptcy will be joined in the petition by his or her spouse. *See supra* § 6.73. However, joint filing is not always necessary to achieve the practical protection of the Bankruptcy Code for both spouses. *See In re Strickland*, 153 B.R. 909 (Bankr. D.N.M. 1993); *Gonzales v. Costanza (In re Costanza)*, 151 B.R. 588 (Bankr. D.N.M. 1993); *Karber*, 25 B.R. at 12 (holding that creditors having community claims against either spouse are precluded by 11 U.S.C. § 524(a)(3) from collecting from community property acquired by either spouse after bankruptcy of only one spouse); *see also* Jennifer L. Street, *The Community Property Discharge in Bankruptcy: A Fair*

*Result or a Creditor's Trap?*, 25 N.M. L. Rev. 229 (1995). One situation calling for a single-spouse filing is that in which the nondebtor spouse has substantial nonmarital property. When only one spouse files, the issue arises whether and under what circumstances a creditor of a family-purpose obligation who has received notice of the debtor spouse's bankruptcy and is subject to the debtor's discharge may recover from the nondebtor spouse.

Marital property acquired by either spouse after the bankruptcy is filed may not be reached in a postpetition action by a pre-petition creditor listed in the bankruptcy. Discharge of the debtor acts as an injunction prohibiting creditors holding community or noncommunity claims from proceeding against the debtor's interest in after-acquired separate or community property (in Wisconsin, nonmarital or marital property) assets. 11 U.S.C. § 524(a). An increase in the value of an exempt community property asset that passes through bankruptcy should also be protected. *See Schmiedel*, 236 B.R. 393. This injunction also necessarily prohibits creditors with community claims from proceeding against the nondebtor spouse's interest in community (marital) property assets acquired after the debtor spouse's bankruptcy. A spouse's interest in community or marital property is an undivided interest in the whole; the spouses' interests in a particular asset may not be severed. This rule has the effect of insulating the interests of both the debtor and the nondebtor spouse in marital property. *But see In re Page*, 171 B.R. 349 (Bankr. W.D. Wis. 1994) (holding that lien was avoided only on debtor's one-half interest in marital property asset).

In bankruptcy actions under chapters other than Chapter 7, the automatic stay may be in effect for long periods of time, thus preventing creditors from recovering before it is known whether the discharge will be granted. *See In re Passmore*, 156 B.R. 595 (Bankr. E.D. Wis. 1993) (indivisibility of spouses' interests necessitated application of automatic stay, as well as subsequent discharge, to both halves of marital property funds). Also, the application of the automatic stay to a nondebtor spouse's marital property assets would prevent the creditor from proceeding against a co-debtor spouse to whom the stay under 11 U.S.C. §§ 1201 and 1301 applies because the marital property acquired after filing would eventually be protected by the discharge under 11 U.S.C. § 524(a)(3). The stay does not apply to recovery of the liable nonfiling spouse's separate property. *Brown v. Kastner (In re Kastner)*, 197 B.R. 620, 624 (Bankr. E.D. La. 1996).

Given that a creditor is not prohibited from recovering nonmarital property of a nonfiling spouse who is liable on a debt for a filing spouse's community claim, the court in *In re Moore*, 318 B.R. 679 (Bankr. W.D. Wis. 2004), held that the creditor did not violate the automatic stay in scheduling a supplemental examination of the debtor's nonfiling wife. The creditor made clear that it was only attempting to obtain information about nonmarital property, and the wife was personally liable with the debtor on the judgment debt. *Cf. Chesnut v. Brown (In re Chesnut)*, 300 B.R. 880 (Bankr. N.D. Tex. 2003) (sanctioning creditor for violation of automatic stay because it proceeded with foreclosure after being notified of debtor's claimed community interest in real estate titled as nonfiling wife's separate property), *rev'd*, 311 B.R. 446 (N.D. Tex. 2004), *rev'd*, 422 F.3d 298 (5th Cir. 2005) (affirming bankruptcy court's decision).

The operation of the injunction under 11 U.S.C. § 524(a)(3) applies to debts incurred by the nondebtor as well as the debtor. That is, the discharge prohibits the nondebtor spouse's creditors holding community claims from proceeding against the nondebtor's or the debtor's after-acquired community property.

➤ **Example.** Assume that spouse A incurs a family-purpose obligation to creditor X and is current with installment payments. A's spouse, B, files a petition in bankruptcy listing X as a creditor; X receives notice. Because A has been making current payments, X does not file a claim in B's bankruptcy estate and does not share in the distribution of all of A and B's nonexempt marital property. After the bankruptcy, A stops making payments. The result is that X may not recover from A's wages or any of A and B's marital property assets that are acquired after the bankruptcy. *See* 11 U.S.C. § 524(a)(3).

The situation in the above example occurred in *Strickland*, 153 B.R. 909, although the filing of a claim was not at issue. The wife hired the plaintiff, an attorney, to represent her in a family-law matter involving a child of a prior marriage, thus incurring a community debt. The husband later filed a voluntary Chapter 7 petition for bankruptcy. The court held that even though the wife did not file a bankruptcy case, 11 U.S.C. § 524(a)(3) precluded the plaintiff from recovering from the spouses' after-acquired community property. *See also Costanza*, 151 B.R. 588. Even though after-acquired community or marital property is protected by discharge, the court in *Strickland*, 153 B.R. at 913, observed that the

nondebtor spouse's creditor could nevertheless recover from the nondebtor spouse's separate property. *See also First Louisiana Bus. & Indus. Dev. Corp. v. Dyson (In re Dyson)*, 277 B.R. 84 (Bankr. M.D. La. 2002) (holding that Chapter 13 discharge also protects both spouses' interest in after-acquired community property); *Kastner*, 197 B.R. at 624 (holding that bankruptcy court had no jurisdiction over creditor's claim against nonfiling spouse's separate property).

The injunction provided for by 11 U.S.C. § 524(a)(3) applies only to community property acquired *after* the commencement of the case; it does not apply to such property owned before the case was filed and still owned by the debtor and his or her spouse after the case is closed. A debtor may continue to own a community property asset before and after bankruptcy in several circumstances. For example, since Wisconsin allows a debtor to choose state or federal exemptions, a community property asset may have qualified as exempt under federal law but not under state law. Nevertheless, 11 U.S.C. § 522(c) protects exempt property from being recovered for most types of debts discharged in the bankruptcy proceedings, and this would make the asset unavailable to creditors after one spouse's bankruptcy. Also, the asset may have increased in value as a result of market factors or the payment of a claim for which the community property asset is collateral. Such appreciation in the value of a community property asset would likewise be community property, unless the asset becomes mixed property under section 766.63, and the increase in value would be community property "acquired" after bankruptcy and protected by the injunction. An exception might be a community property asset abandoned by the trustee under 11 U.S.C. § 554, and such an asset could be subject to recovery after bankruptcy. *See also Sanwa Bank Cal. v. Chang*, 105 Cal. Rptr. 2d 330 (Ct. App. 2001) (holding that asset initially owned as community property, fraudulently transferred to wife as her separate property before husband's bankruptcy, and not administered by the trustee, was community property and not protected by discharge injunction from recovery by creditor).

## **(2) After Termination of Marriage by Death or Dissolution [§ 6.109]**

If the marriage is dissolved after one spouse receives a discharge and the nondebtor spouse receives former marital property assets that were acquired after the bankruptcy or were exempt in the bankruptcy, then the

injunction under 11 U.S.C. § 524(a)(3) no longer prohibits a creditor from proceeding against the nondebtor to recover those assets. *See* Wis. Stat. § 766.55(2m). This result occurs because 11 U.S.C. § 524(a)(3) prohibits recovery only of “property of the debtor of the kind specified in section 541(a)(2)” —namely, assets classified as marital property. After dissolution, former marital property assets are no longer classified as marital property in the hands of a former spouse. *Von Burg v. Egstad (In re Von Burg)*, 16 B.R. 747 (Bankr. E.D. Cal. 1982) (holding that discharge injunction does not protect assets of personally obligated nondebtor former spouse because spouses were divorced before filing and former wife’s assets were not community property acquired after commencement of case). The purpose of a discharge is to protect the debtor’s “fresh start,” not to provide a fresh start for a former spouse who does not file a bankruptcy case. Commenting on the potential effect of divorce of a debtor previously protected by the other spouse’s discharge, the court in *Costanza* observed, “[I]f he does not treat her better than his creditors, she will, by divorcing him, deny his discharge.” 151 B.R. at 590.

Similar reasoning applies after the death of the discharged debtor spouse. Former marital property owned by the surviving spouse is no longer property described in 11 U.S.C. § 541(a)(2) (community property), and the injunction under 11 U.S.C. § 524(a)(3) does not apply. *See also* Wis. Stat. § 859.18(3)(b) (providing for recovery from surviving spouse’s marital property).

Outside the bankruptcy context, the income of a surviving obligated spouse is available to satisfy obligations resulting from an extension of credit or a tax obligation to the state. Wis. Stat. § 859.18(3)(a); *see infra* ch. 12. Such income is not classified as marital property after the death of the obligated spouse, but it appears that the surviving nondebtor spouse’s income is recoverable by a creditor of such an obligation, even though the obligation was discharged in the bankruptcy of the deceased obligated spouse.

**b. Denial of Discharge or Dischargeability of  
Debt of Debtor or Denial of Hypothetical  
Discharge or Dischargeability of Debt of  
Debtor's Spouse [§ 6.110]**

Under certain circumstances, a discharge may be unavailable to a debtor, or certain debts may not be discharged. *See* 11 U.S.C. §§ 727, 523. The grounds for completely denying a discharge relate primarily to misconduct during the bankruptcy or to the receipt of a discharge less than six years before filing. 11 U.S.C. § 727. Also, the discharge of a particular debt may be disallowed because of the type of debt (such as certain student loans or debts relating to support of dependents) or because of fraud, use of a false financial statement, or other intentional wrongdoing committed by the debtor in connection with incurring the obligation. 11 U.S.C. § 523(a), (c).

Obligations that are nondischargeable because they are in a particular category, such as support of dependents, may be recovered at any time, provided that the action does not violate the automatic stay under 11 U.S.C. § 362. Exceptions to discharge under 11 U.S.C. § 523(a)(2), (4), (6), and (15) (obligations incurred by fraud, use of a false financial statement, certain intentional torts, and certain family obligations other than those for support) must be determined by the bankruptcy court in an adversary proceeding commenced by the creditor within the time allowed. *See* Fed. R. Bankr. P. 4007; 11 U.S.C. § 523(c). If no such action is commenced, the debt is discharged. 11 U.S.C. § 523(c); *see also* 11 U.S.C. §§ 1141(d), 1228(a), 1328(c). *But see* 11 U.S.C. § 1328(a) (debts of kind specified in 11 U.S.C. § 523(a)(2), (4), (6), and (15) are not excepted from Chapter 13 discharge).

Section 524(a)(3) of the Bankruptcy Code states that in a case involving community property, the injunction prohibiting recovery by a creditor holding a community claim applies to all after-acquired separate and community property assets of the debtor. There is, however, an exception for those creditors holding community claims that have been excepted from discharge under 11 U.S.C. §§ 523 and 1328(a) or that would have been excepted if the debtor's spouse had filed a bankruptcy petition on the same day as the filing spouse, whether or not the discharge based on the community claim is waived. 11 U.S.C. § 524(a)(3), (b)(2). Therefore, a creditor wishing to object to the discharge of its debt may base the objection on acts committed by the



debtor's spouse as well as by the debtor. 11 U.S.C. § 524(a)(3), (b)(2). This is because it would be inequitable to allow a spouse who incurred an obligation by fraud or other wrongful act to obtain the advantage of the bankruptcy discharge through the discharge obtained by his or her spouse. Absent this provision, the wrongdoer would be insulated by the injunction in 11 U.S.C. § 524(a)(3) against a creditor's attempting to obtain satisfaction from marital property acquired after the bankruptcy filing. *See supra* §§ 6.107–.109.

The court in *Grimm v. Grimm*, 82 B.R. 989 (Bankr. W.D. Wis. 1988), analyzed the Act's effect on a creditor's right to collect after-acquired marital property for a nondischargeable debt incurred by one spouse. There was a judgment in state court against the husband for conversion, and the wife, a joint debtor, asked to be dismissed as a party in the adversary proceeding filed to determine dischargeability. The court noted that if the debt were found nondischargeable, the injunction of 11 U.S.C. § 524(a)(3) would not protect either spouse's interest in after-acquired marital property. *Id.* at 993–94. Furthermore, the creditor had a community claim and could share in either spouse's estate. *Id.* at 991–92; *see also supra* §§ 6.92–.104. Since the creditor's right to recover would not be impaired and there was no allegation of personal liability, the court dismissed the wife as a party. *Grimm*, 82 B.R. at 994; *see also Soderling*, 998 F.2d 730 (holding that restitution for federal crime was nondischargeable as to separate and community property); *Case v. Maready (In re Maready)*, 122 B.R. 378 (B.A.P. 9th Cir. 1991) (holding that nondischargeable debt of one spouse may be satisfied from after-acquired community property only if debt was community claim; no notice to nondebtor spouse necessary to determine if debt was nondischargeable); *Arcadia Farms Ltd. v. Rollinson (In re Rollinson)*, 322 B.R. 879 (Bankr. D. Ariz. 2005) (concluding that wife's nondischargeable debt, memorialized by promissory note signed by both spouses that established nondischargeable debt as community claim, subjected all community property to recovery after discharge); *Brown v. Kastner (In re Kastner)*, 197 B.R. 620 (Bankr. E.D. La. 1996) (holding that nonfiling husband's debt for fraud and embezzlement was recoverable from both spouses' after-acquired community property); *Sophos v. Hibbs (In re Hibbs)*, 161 B.R. 259 (Bankr. C.D. Cal. 1993) (holding that creditor of nondischargeable debt against husband could reach both spouses' postpetition community property); *Midi Music Ctr., Inc. v. Smith (In re Smith)*, 140 B.R. 904 (Bankr. D.N.M. 1992); *Meneley Motors, Inc. v. Giantvalley (In re Giantvalley)*, 14 B.R. 457 (Bankr. D. Nev. 1981) (holding that nondischargeable debt could be enforced

against same property that would have been available under state law if bankruptcy had not occurred); *Williams v. Bernardelli (In re Bernardelli)*, 12 B.R. 123 (Bankr. D. Nev. 1981).

If a creditor of the nondebtor spouse has a basis for objecting to the discharge of a debt on account of conduct by the nondebtor spouse that would have prevented discharge of the debt if the nondebtor spouse had been in bankruptcy, the creditor must file the objection in the bankruptcy of the debtor spouse within the time limits set for the debtor—that is, 60 days from the first date set for the meeting of creditors. 11 U.S.C. § 524(b)(2)(B); Fed. R. Bankr. P. 4004; *Karber*, 25 B.R. 9. *But see Costanza*, 151 B.R. at 589 n.3 (declining to determine whether 60-day time limit applied to hypothetical discharge). This concept is referred to as an objection to the *hypothetical discharge*. If the objection is successful, the claim is not subject to the discharge injunction. 3 *Collier*, *supra* § 6.72, ¶ 524.01.

➤ **Practice Tip.** The above rule again demonstrates the importance of creditors' knowing the names and addresses of, and other pertinent information about, debtors' spouses.

The nondebtor spouse is a necessary party to an action by a creditor objecting to the hypothetical discharge of the nondebtor spouse. *Judge v. Braziel (In re Braziel)*, 127 B.R. 156 (Bankr. W.D. Tex. 1991). If the spouses have filed separate bankruptcy cases, the objection to the dischargeability of a debt should be brought only in the case of the alleged wrongdoer. *Smith*, 140 B.R. 904. However, if the alleged wrongdoer has filed a Chapter 13 bankruptcy and the innocent spouse has filed a Chapter 7 bankruptcy, the action should be brought in the innocent spouse's case. *See id.*

If the discharge is denied for a particular obligation, the injunction under 11 U.S.C. § 524(a)(3) does not prevent the creditor from recovering after-acquired community property, even if the spouse who did not incur the obligation was granted a discharge, as was the case in *Valley National Bank of Arizona v. LeSueur (In re LeSueur)*, 53 B.R. 414 (D. Ariz. 1985). The debtors had filed a joint bankruptcy petition, and the court found that only the husband's debt to the plaintiff creditor was nondischargeable by reason of a false financial statement. The wife was granted a discharge. Nevertheless, the court found that the wife's post-petition community property would be subject to recovery even though the wife was not at fault. Citing 3 *Collier on Bankruptcy* ¶ 524.01, at

524–11 (15th ed. 1985), the court stated that “the Code’s clear policy is that the economic sins of either spouse shall be visited upon the community when a discharge is denied.” *LeSueur*, 53 B.R. at 416. The court also noted that the denial of a discharge as to the husband did not change the obligation to a separate obligation (analogous to a nonfamily-purpose obligation in Wisconsin), which under applicable state (Arizona) law would protect a portion of the wife’s community property. The loan in question, even though procured by fraud, had been incurred for various family purposes, and it would have been recoverable from all community property if no bankruptcy had intervened. *Id.* at 415–16; *see also Soderling*, 998 F.2d 730 (9th Cir. 1993); *Sophos v. Hibbs (In re Hibbs)*, 161 B.R. 259 (Bankr. C.D. Cal. 1993).

Debtors and spouses may not alternate filing every three years to avoid the six-year prohibition against repeated discharges under 11 U.S.C. § 727(a)(8). Section 524(b)(1) of the Bankruptcy Code states that the injunction against a creditor’s proceeding to collect community property acquired after the commencement of the case to satisfy a discharged obligation does not apply if the debtor’s spouse (1) filed a bankruptcy petition within six years of the debtor’s filing and (2) did not receive or would not have received a discharge had the spouse filed at the same time as the debtor. The objection to the spouse’s hypothetical discharge under this section must be filed within the time limits set for objecting to the debtor’s discharge. 11 U.S.C. § 524(b)(2)(B); *Seattle First Nat’l Bank v. Marusic (In re Marusic)*, 139 B.R. 727 (Bankr. W.D. Wash. 1992) (denying debtor discharge because debtor’s spouse had received discharge within six years and would have been denied discharge under 11 U.S.C. § 727(a)(8)).

➤ **Note.** When the *Marusic* case was decided, the law provided that a debtor would be denied a discharge in a Chapter 7 bankruptcy proceeding if the debtor had received a discharge in an earlier bankruptcy case within six years of filing the subsequent case. BAPCPA extended this period to eight years. 11 U.S.C. § 727(a)(8).

### **c. Claims of Spouses and Dependents [§ 6.111]**

A support obligation owed to a spouse, a former spouse, or minor children is not dischargeable in bankruptcy. 11 U.S.C. § 523(a)(5). An obligation constituting a debt or division of property is dischargeable only under Chapter 13. *See* 11 U.S.C. §§ 523(a)(15), 1328(a)(2). If a

debtor seeks to discharge an obligation arising out of section 766.70, the analysis used to determine the dischargeability is the same whether the obligation is to a spouse or a former spouse (i.e., whether the obligation is for support or for property division under bankruptcy law). *See Sommer & McGarity, supra* § 6.6, ch. 6.

## 6. Reaffirmations [§ 6.112]

A debtor may reaffirm a debt under 11 U.S.C. § 524(c), thereby creating a new enforceable promise to pay. The newly created obligation may or may not fall within the family-purpose doctrine. If it does, then marital property acquired after the bankruptcy may be recovered to satisfy the new obligation. The means of determining whether a family purpose exists is the same for a reaffirmation as for any other obligation when it becomes necessary to determine the category of obligation under section 766.55(2). In community property states, the renewal of a community obligation has been found presumptively to obligate the community; however, the reaffirmation is subject to scrutiny to determine whether a family purpose existed at the time of the reaffirmation, not at the time the original debt was incurred. *See Gannon v. Robinson*, 371 P.2d 274 (Wash. 1962) (holding that reaffirmation of debtor's divorce obligation to former wife was ineffective because statutory provisions for reaffirmation agreements were not followed); *see also In re Ellis*, 103 B.R. 977, 981 (Bankr. N.D. Ill. 1989) (same); *Lumby v. Lumby*, 116 Wis. 2d 347, 341 N.W.2d 725 (Ct. App. 1983) (same). For example, the reaffirmation of a secured debt that allows the debtor to keep the family car probably would be regarded as a family-purpose debt, allowing the creditor to collect from all marital property. Wis. Stat. § 766.55(2)(b). The reaffirmation of an unsecured debt may also have a family purpose under certain circumstances, such as when the debt is to a family member or was co-signed by a family member.

➤ **Comment.** It is not clear whether the debtor's spouse may effectively reaffirm a debt, with the result that 11 U.S.C. § 524(a)(3) will not apply to the debt and the creditor may recover marital property acquired after the case is commenced. The requirements for a binding reaffirmation agreement under 11 U.S.C. § 524(c)–(d) apply only to the debtor, and it appears that the nonfiling spouse could not fulfill these requirements.

## **VI. Sample Complaint for Damages [§ 6.113]**

### **A. In General [§ 6.114]**

The following is a sample complaint for damages in which it is alleged that only one spouse is personally liable, but recovery is sought from marital property. It is a sample only and does not purport to be all-inclusive. Each pleading must be tailored to the circumstances of the parties.



4. Defendant Fred Smith is the sole proprietor of a business known as Smith Electrical Contracting. His business address is 818 Industrial Park Boulevard, Milwaukee, Wisconsin 53299. His business is providing commercial and residential electrical contracting services.

5. On January 2,\_\_\_\_, plaintiff and defendant Fred Smith entered into a written contract, a copy of which is attached to this complaint as Exhibit A.

6. Under the terms of the contract, defendant Fred Smith agreed, for the contract price of \$10,000, to provide electrical service for a family room addition being built on plaintiff's house. The work was to have been completed by March 1,\_\_\_\_.

7. Defendant Fred Smith failed to perform the work in a skillful manner. The wiring was completely inadequate for the air conditioning system, and there were fewer outlets and fewer circuits than agreed on in the contract. Defendant Fred Smith failed after several attempts to correct the situation.

8. As a result of defendant Fred Smith's breach, plaintiff was forced to hire another electrical contractor to correct and complete the work, at a cost of \$15,000.

9. This obligation is incurred by defendant Fred Smith in the interest of defendant's marriage and family.

WHEREFORE, plaintiff requests that the court:

1. Grant judgment to plaintiff against defendant Fred Smith, individually, in the amount of \$15,000;

2. Declare this obligation to be in the interest of the marriage and the family of defendants Fred Smith and Jane Doe Smith;

3. Declare that any marital property held by Fred Smith or Jane Doe Smith or both be available for satisfaction of this obligation; and

4. Grant plaintiff such other relief as is appropriate under the circumstances.

Dated: \_\_\_\_\_.

Jones & Kelly  
Attorneys for Plaintiff

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Michael R. Kelly  
State Bar No. 000002

819 First St.  
Milwaukee, WI 53299  
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## Marriage Agreements

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## **I. Scope of Chapter [§ 7.1]**

This chapter focuses on the different types of contractual agreements spouses may create to define their property rights. The formal requirements for marriage agreements, the subject matter that such agreements may involve, and various planning considerations are discussed. In addition, the chapter includes sample marriage agreement forms.<sup>1</sup>

## **II. Marriage Agreements in General [§ 7.2]**

In most states, the right of spouses to enter into contractual arrangements affecting their economic relationship and their property has been recognized historically as a matter of either common law or statutory law.

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189, and all references to the United States Code (U.S.C.) and Internal Revenue Code (I.R.C.) are current through Public Law Number 111-166 (excluding Pub. L. Nos. 111-148, -152, and -159) (May 17, 2010). Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

These contractual arrangements can be loosely divided into (1) agreements entered into before or during marriage primarily to govern the spouses' property rights and tax consequences after the death of one of them, and perhaps also their financial relationship during marriage, and (2) property settlement agreements or stipulations entered into in immediate contemplation of the dissolution of the marriage (or during the pendency of an action for dissolution) to fix the spouses' support, maintenance, and property rights. *See, e.g., Ray v. Ray*, 57 Wis. 2d 77, 82, 203 N.W.2d 724 (1973). In recent years, there has been an increasing tendency to blur the distinction between the two categories. This occurs when provisions for support, maintenance, and asset division in the event of separation or divorce are included in the first type of agreement even though no separation or divorce is immediately contemplated. *See infra* §§ 7.107, 7.133–.140.

➤ **Note On Terminology.** Marriage agreements entered into before marriage are variously referred to as *premarital* or *prenuptial agreements*. Those entered into after the parties are married are referred to as *postmarital* or *postnuptial agreements*. For convenience, all agreements affecting the spouses' property rights during marriage or at death (as distinguished from dissolution property settlement agreements or stipulations), whether entered into before or during marriage, are generically referred to as *marriage agreements* in this chapter. The term *marital property agreement* as defined in section 766.01(12) is included in the generic reference.

➤ **Note.** In some states, including those adopting the Uniform Marital Property Act in its original (1983) version, the requirements for premarital and postmarital agreements differ. Requirements for Wisconsin marital property agreements are discussed in sections 7.15–.70, *infra*.

The term marital property agreement refers specifically to an agreement that complies with the requirements of section 766.58. The term also includes anticipatory marital property agreements described in section 766.585, *see infra* § 7.26, and various statutory property classification agreements described in sections 766.587, 766.588, and 766.589, *see infra* §§ 7.71–.98. With the exception of anticipatory marital property agreements under section 766.585 and the now-expired statutory individual property classification agreements under section 766.587, the statutory provisions concerning marital property agreements



apply only to agreements entered into after December 31, 1985, the day before the effective date of the Wisconsin Marital Property Act, 1983 Wis. Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or the Wisconsin Marital Property Act]. Marital property agreements are discussed in detail in sections 7.3–.118, *infra*.

Marriage agreements have been and will continue to be used in a wide variety of situations by married persons as well as by persons about to marry. A partial checklist of these situations follows.



***Checklist: Common Situations  
in Which Marriage Agreements Are Used***

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- ☐ In a second marriage when one or both of the parties have property, have children by a prior marriage, and desire to leave all or most of their estates (especially that portion acquired before remarriage) to their respective children
- ☐ In a first or second marriage when one party has received or will receive substantial inherited wealth or an interest in a closely held business
- ☐ In a marriage later in life when children are not involved, but when one or both of the parties have significant responsibilities for the care and support of a parent or other dependent relative
- ☐ When there is a need to clarify the terms of a prior marriage agreement between the spouses that arguably does not address itself to the community property system contained in the Wisconsin Marital Property Act.
- ☐ When one or both of the spouses are parties to buy-sell arrangements with respect to business assets
- ☐ When the parties wish to maintain ownership of their property based on title (or alternatively to provide for the classification of their property as individual property as defined in the Act), and also, to the extent possible, to

maintain a system of debt satisfaction based on who incurred the obligation (an “opt-out” agreement)

- ☐ When the parties wish to make the marital property provisions of the Act applicable to most or all of their existing property after the determination date (an “opt-in” agreement)
- ☐ When the parties wish to classify their property to simplify the probate of their estates
- ☐ When the parties wish to classify only certain assets, provide debt satisfaction rules for certain liabilities, or define management and control rights concerning certain assets, particularly when specific bequests of property or specific nonprobate assets will be left to third persons at the death of either of the parties
- ☐ When the parties prefer a nonprobate transfer of their property at death through a will substitute agreement, rather than a transfer by will or intestacy

### **III. Marital Property Agreements Under the Act [§ 7.3]**

#### **A. In General [§ 7.4]**

The enactment of statutory provisions relating to marriage agreements (referred to as *marital property agreements* in the Act) reveals a legislative intent to define the attributes and requirements of such agreements and to promote greater contractual freedom between married persons. June Miller Weisberger, *The Wisconsin Marital Property Act: Highlights of the Wisconsin Experience in Developing a Model for Comprehensive Common Law Property Reform*, 1 Wis. Women’s L.J. 5, 60–68 (1985), reprinted in 13 Community Prop. J., July 1986, at 1, 33–38.

## **B. Freedom to Vary Effect of Chapter 766 by Contract** **[§ 7.5]**

### **1. In General [§ 7.6]**

The right of married persons (or persons about to marry) to vary the effect of chapter 766 contractually is expressly recognized in section 766.17(1). The comment to section 3 of the Uniform Marital Property Act (UMPA), *reprinted in* app. A, *infra*, from which section 766.17(1) is derived, makes it clear that this message is to be delivered “early and emphatically.” The comment further states:

Thus a couple may opt-out, opt-in, or do both in part. Custom-tailored marital property regimes are possible. The Act [UMPA] permits a couple to move its marital economics from status to contract and encourages a type of interspousal contractual freedom little known in common law states. It is important to the operation of the Act [UMPA] that the significance of this section be carried through to the use and application of its various provisions.

UMPA § 3 cmt.

The comment specifically singles out the following areas as suitable subjects for contractual modification of the Act’s effects:

1. Classification of property generally;
2. Management and control;
3. Classification of life insurance;
4. Classification of employee benefits;
5. Disposition of property at the dissolution of the marriage; and
6. Disposition of property at death.

*See id.* The list is not intended to be exhaustive. *Id.* It is with this fundamental UMPA principle in mind that one approaches marital property agreements under the Act. See sections 7.28–.38, *infra*, for a detailed discussion of the permissible subject matter of marital property agreements.

Although the Act creates its own complete system of property classification for married persons, *see supra* ch. 2, it also specifically contemplates that additional forms of property ownership may be created by the agreement of the spouses. *See* Wis. Stat. § 766.17(1). As the comment to UMPA section 3 notes, “The Act’s [UMPA’s] property system applies if it is not changed,” and “[c]ustom-tailored marital property regimes are possible.” Given the broad language in section 766.58(3)(a)–(h), *see infra* §§ 7.28–.38, there appears to be clear authority for spouses to adopt (or continue to use) common law forms of ownership, such as solely owned property, tenancy in common, and joint tenancy with right of survivorship, after the determination date. *See* Wis. Stat. Ann. § 766.60(4)(b) Legis. Council Notes—1985 Act 37, §§ 124–126 (West 2009) (“Should spouses wish to have the incidents of traditional joint tenancy or tenancy in common, regardless of the classification of the property, they may do so by marital property agreement.”).

➤ **Query.** May a marital property agreement vary the effect of statutory provisions *outside* chapter 766? Section 766.17(1) states that, with certain exceptions, a marital property agreement may vary the effect of chapter 766. 1985 Wisconsin Act 37 [hereinafter 1985 Trailer Bill] did not broaden the reference in section 766.17(1) to include portions of the Wisconsin Statutes beyond chapter 766, even though it transferred the important deferred marital property provisions of former section 766.77 from chapter 766 to chapter 861. 1997 Wisconsin Act 188 [hereinafter 1998 Probate Code Revision Bill] brought clarification to this issue by adoption of section 861.10 as part of the statutes dealing generally with the deferred marital property elective share. Section 861.10(1) specifically provides that the right to elect a deferred marital property elective share may be waived by a surviving spouse in whole or in part, either before or after marriage, by a provision in a marital property agreement that is enforceable under section 766.58. The statute further provides, in section 861.10(2), that a waiver of “all rights” (or equivalent language) in a present or prospective spouse’s property or estate, or in a complete divorce property settlement agreement, operates as a waiver of all rights to the deferred marital property elective share. Less clear is whether the other rights, allowances, and exemptions contained in subchapter III of chapter 861, Wis. Stat. §§ 861.17–.43, are subject to variance or waiver by marital property agreement. Section 766.58(3)(h), which permits spouses to agree in a marital property agreement about “[a]ny other matter affecting either or both

spouses' property not in violation of public policy or a statute imposing a criminal penalty," may be sufficient to permit the parties to negate, modify, or expand the other rights, allowances, and exemptions in subchapter III of chapter 861, as well as statutory provisions in other chapters that are of economic significance. This interpretation is consistent with the UMPA section 3 comment that specifically envisages contractual modification of the Act with respect to dispositions of property at death.

➤ **Note.** It should be borne in mind that marital property agreements are not the only method of reclassifying property under the Act. Gifts, unilateral statements under section 766.59, written consents under section 766.61(3)(e), written instruments conveying an interest in a security as defined in section 705.21(11), and even conveyances are all alternative means to accomplish reclassifications. Wis. Stat. § 766.31(10).

## **2. Limitations on Freedom to Vary [§ 7.7]**

### **a. In General [§ 7.8]**

The freedom of spouses to arrange the economic affairs of their marriage by contract is not without limitation. Spouses are subject to six specific statutory exceptions referred to in subsections 766.17(1) and (2) and in subsections 766.58(2) and (14). These exceptions, which are discussed in sections 7.9–14, *infra*, may not be varied by marital property agreement. All but two of these exceptions (the protection of a creditor's right to satisfaction of obligations at the death of a spouse, and limitations on the effect of an agreement for Wisconsin income tax purposes) are found in more or less similar form in UMPA.

### **b. Duty of Good Faith [§ 7.9]**

The duty of a spouse to act in good faith with respect to matters involving marital property or other property of the other spouse may not be varied by a marital property agreement. *See* Wis. Stat. § 766.15. If the marital property agreement provides that the spouses will have no marital property, the effect of this section is substantially diminished, because one spouse will have little occasion to act in regard to the property of the other.

### **c. Protection of Creditors' Interests During Marriage [§ 7.10]**

Under sections 766.55(4m) and 766.56(2)(c), a provision in a marital property agreement will not bind a creditor who does not have actual knowledge of the provision (or is not furnished a copy of the agreement) at the time the obligation to the creditor is incurred, or in the case of an open-end credit plan, at the time the plan is entered into.

This limitation makes it virtually impossible for the spouses to restrict in advance the right of involuntary creditors (such as tort-judgment creditors or governmental entities imposing fines or penalties) to reach all property that would have been classified as marital property absent the agreement, because ordinarily such creditors will have no actual knowledge of the terms of the marriage agreement. The provision works similarly for voluntary creditors unless the creditor has actual knowledge of the agreement or a copy is provided to the creditor by the credit applicant before the credit is granted or an open-end credit plan is entered into. *See* Wis. Stat. §§ 766.55(4m), .56(2)(c); *see also Bank One, Appleton, NA v. Reynolds*, 176 Wis. 2d 218, 500 N.W.2d 337 (Ct. App. 1993). The circumstances under which marital property agreements may limit the property that the federal and Wisconsin taxing authorities may reach in satisfaction of tax obligations are discussed in chapter 9, *infra*.

The efficacy of a marital property agreement to prevent inclusion of a nondebtor spouse's individual property assets in the debtor spouse's bankruptcy estate was illustrated in *Rinehart v. Meek (In re Grady)*, 128 B.R. 462 (Bankr. E.D. Wis. 1991), although the effect of section 766.55(4m) was not discussed in the opinion. The spouses had entered into a postmarital agreement that declared their intention to opt out of the Act and to classify all assets titled in their individual names (including earnings, income, and appreciation) as solely owned property treated as though they were unmarried. When the spouses divorced, their divorce settlement agreement and judgment allocated assets consistent with the ownership of the assets under the agreement.

The former husband then filed a bankruptcy petition. The bankruptcy trustee sought to recover the property received by the former wife on the ground that the divorce decree effected a transfer that was intended to hinder, delay, or defraud the former husband's creditors within the

meaning of section 242.04(1)(a), a provision of the Uniform Fraudulent Transfer Act. The trustee argued that because the former wife had commingled her earnings with inherited and gift property received from her family during the marriage, all of the funds had become marital property under section 766.63 and were therefore reachable by the former husband's creditors. *Id.* at 464–65. The bankruptcy court rejected this argument, holding that a marital property agreement may vary the effect of the Wisconsin Marital Property Act and adopt property classifications that preclude the necessity of tracing. Accordingly, the court held that the trustee had failed to prove that the former husband had any marital property interest in the assets awarded to the former wife that could be reached for the bankruptcy estate. Thus, there was no transfer for the trustee to avoid and recover for the bankruptcy estate.

For further discussion of the effect of classification of property by marital property agreement upon bankruptcy proceedings, see chapter 6, *supra*. See section 6.37, *supra*, for additional discussion about what suffices to give a creditor notice or actual knowledge of a marital property agreement. For a specific discussion of statutory provisions applicable to the satisfaction of obligations at the death of a spouse, see section 7.12, *infra*.

#### **d. Protection of Bona Fide Purchasers' Interests** **[§ 7.11]**

A marital property agreement may not vary the effect of the Act's provision protecting the interests of a bona fide purchaser who purchases marital property from a spouse having the right of management and control. *See* Wis. Stat. § 766.57(3). This provision is included to enhance commercial certainty under a system in which the holding of title no longer necessarily indicates ownership rights. If the marital property agreement provides that the spouses have no marital property, this exception has little consequence.

**e. Protection of Creditors' Interests at Death  
When Assets Are Transferred by Will  
Substitute Agreement [§ 7.12]**

A marital property agreement may not vary the effect of the spousal debt satisfaction scheme established by section 859.18 except in limited circumstances. This limitation on the scope of marital property agreements is not found in UMPA. *See* Wis. Stat. § 859.18(2), (6). The applicable statutes are complex, and their relationship is not entirely smooth. Nonetheless, it appears that the intention of section 859.18(6) is to emphasize that assets transferred outside the probate estate by will substitute agreement remain available for debt satisfaction even though these assets are not otherwise subject to the probate claims procedures of chapter 859.

➤ **Note On Terminology.** In the following discussion, a person to whom an obligation is owed by a spouse is referred to as a creditor. The term *creditor* is used here in its general sense and is not to be confused with the defined term in section 766.01(2r) or section 859.18(1)(b).

Section 766.55(8) states that after the death of a spouse, property is available for satisfaction of obligations as provided in section 859.18. Section 766.17(2) provides that the effect of a marital property agreement on property available for satisfaction of an obligation after the death of a spouse is governed by section 859.18(6). The latter subsection states that a provision in a marital property agreement that provides for the disposition of either or both of the spouses' property upon the death of a spouse (i.e., a will substitute provision) does not affect property available for satisfaction of obligations under section 859.18 unless (1) the property was not available for satisfaction under the marital property agreement while both spouses were alive; and (2) the agreement is binding on the creditor under section 766.55(4m) or section 766.56(2)(c) because the creditor had actual knowledge of the provision or was furnished a copy of the agreement. Thus, unless the property was unavailable to the creditor while both spouses were alive because the agreement was binding on the creditor, the basic rule for satisfaction of obligations at death under section 859.18 continues to apply. The basic rule of section 859.18 is as follows: property that, but for the death of the spouse, would have been available under section 766.55(2) for satisfaction of an obligation continues to be available for satisfaction,



with several significant exceptions noted in the statute. *See* Wis. Stat. § 859.18(2)–(5).

Property classified by agreement as one spouse's individual or solely owned property would not generally be available to a creditor under section 766.55(2) to satisfy an obligation incurred by the other spouse under any of the following circumstances:

1. If the creditor had actual knowledge of the provisions of the marital property agreement when the obligation to the creditor was incurred or the open-end plan was entered into;
2. If the existence of a currently effective marital property agreement was disclosed to the creditor and the creditor was provided with a copy of the agreement before credit was granted or the plan entered into; or
3. If the creditor consented in writing to be bound by the agreement's provisions.

*See* Wis. Stat. §§ 766.55(4), (4m), .56(2)(c). These same rules should hold true upon the death of one of the spouses to protect special debt-satisfaction arrangements between the spouses in a marital property agreement.

➤ **Comment.** Section 859.18(6) makes clear that property not available for debt satisfaction under the terms of a marital property agreement while both spouses were alive does not become available upon the death of one of the spouses if the creditor was bound by the provisions of the agreement under the notice statutes, sections 766.55(4m) and 766.56(2)(c). Interestingly, the statute does not mention creditors who are bound because they consented in writing to be bound by the agreement provision under section 766.55(4), although there is no policy reason not to continue to treat such a creditor as bound following the death of one of the spouses. Clearly, however, the spousal debt-satisfaction scheme of section 859.18 may not be displaced by a marital property agreement that (1) the creditor did not have actual knowledge of when the obligation arose, (2) was not disclosed to the creditor and a copy provided before credit was granted or the plan entered into, or (3) the creditor did not consent to in writing.

#### **f. Protection of Child's Right to Support [§ 7.13]**

A marital property agreement may not adversely affect the right of a child to support. *See* Wis. Stat. § 766.58(2). This limitation is consistent with the law before the adoption of the Act: under pre-Act law, an agreement by a spouse that limited his or her legal responsibilities to support a child probably would be declared void as against public policy. *See* Wis. Stat. § 49.90(1m), (2) (providing that each parent has equal obligation to support his or her minor children and that any parent who fails to provide maintenance is subject to court order to compel such maintenance); *see also* Wis. Stat. § 765.001(2). For a discussion of the modification of spousal support obligations by agreement, see sections 7.34 and .133–.140, *infra*. For a discussion of the duty to support minor children, see chapter 5, *supra*, and chapter 11, *infra*.

➤ **Note.** The Act does not bar a marital property agreement from providing that the income and assets of a new spouse are not available for satisfaction of child support obligations with respect to the other spouse's children by a former marriage. Nor does the Act prohibit excluding the new spouse's income and assets from consideration in determining the amount of support the other spouse's children by a prior marriage are entitled to receive.

#### **g. Limitations on Marital Property Agreement's Effect for Wisconsin Income Tax Purposes [§ 7.14]**

The effect of a marital property agreement for state income tax purposes is limited as set forth in chapter 71. *See* Wis. Stat. § 766.58(14). The chief limitation provides that a marital property agreement does not affect the determination of either (1) the income that is taxable by the state of Wisconsin or (2) the person who is required to report taxable income to the state of Wisconsin during any period that one or both of the spouses are not domiciled in Wisconsin. *See* Wis. Stat. § 71.10(6)(c). If both spouses are domiciled in Wisconsin, the agreement will not affect these issues unless it is filed with the Wisconsin Department of Revenue (DOR) before an assessment is issued. *Id.*

The inability of a marital property agreement to operate retroactively, particularly in the year of the dissolution of a marriage, constitutes a major practical limitation on the effectiveness of marital property agreements for Wisconsin income tax purposes. This and other limitations on the effectiveness of marital property agreements for income tax purposes are found not only in the Wisconsin Statutes, but also in the DOR's administrative rules and information releases. *See, e.g.,* Wisconsin Dep't of Revenue, Publ'n No. 113, *Federal and Wisconsin Income Tax Reporting Under the Marital Property Act* (Jan.. 2010), at <http://www.dor.state.wi.us/pubs/pb113.pdf>.

## **C. Requirements for Marital Property Agreements**

### **[§ 7.15]**

#### **1. In General [§ 7.16]**

Marital property agreements are the primary statutory vehicle for carrying out the “almost unlimited contractual freedom” granted to spouses regarding their property and the economics of their marriage. UMPA § 10 cmt. The comment to UMPA section 10 contemplates that a marital property agreement “will usually be a postmarital agreement” and that there may be “many of them made at numerous times during a marriage.” The comment also recognizes that premarital agreements are on a different footing and that once the spouses have outlined their respective rights and responsibilities in a premarital agreement, such an agreement is likely to be changed infrequently, if at all.

#### **2. Formal Requirements [§ 7.17]**

##### **a. Document [§ 7.18]**

Section 766.58(1) sets forth the formal requirements of marital property agreements. Such an agreement must be a “document” signed by both spouses. Wis. Stat. § 766.58(1).

### **b. Appropriate Parties [§ 7.19]**

Only spouses may be parties to a marital property agreement. Wis. Stat. § 766.58(1). Thus, contracts involving the spouses and third parties, such as land contracts, mortgages, bank or brokerage accounts, and buy-sell agreements, are not included within the definition of a marital property agreement. On the other hand, a trust agreement executed and self-trusted by both spouses (with no third party involved) may meet the requirements of section 766.58(1).

A guardian of a spouse's estate may execute a marital property agreement with the ward's spouse, or with the ward's intended spouse. Wis. Stat. § 54.20(2)(h). This authority may only be exercised with the court's prior written approval following petition. Wis. Stat. § 54.20(2)(intro).

➤ **Comment.** Section 54.20(2)(h) specifically prohibits a guardian from making, amending, or revoking a will for the ward. It is not clear what effect this rule has on a guardian's ability to enter into a will substitute marital property agreement with the other spouse purporting to dispose of either the incompetent spouse's property, or the property of both spouses, at death. The legislative history of the predecessor to this provision indicates that a guardian's authority "includes but is not limited to" the power to "create, for the benefit of the married person or others, revocable or irrevocable trusts of marital property and other than marital property which may extend beyond . . . the life of the married person." 1985 Wis. Act 37, § 184. For links to this Act and others amending the Wisconsin Marital Property Act, see appendix B, *infra*. Nor is it clear whether a person who is the guardian of the estate of his or her spouse may participate in the making (or amendment) of a marital property agreement that works to his or her benefit. Under these circumstances, the court may appoint a temporary guardian under section 54.50 to act for the incompetent spouse.

### **c. Consideration [§ 7.20]**

A marital property agreement is enforceable without consideration. Wis. Stat. § 766.58(1).

Although no consideration is required to support a marital property agreement under section 766.58(1), it has been held that consideration or “value” is required for the agreement to apply in bankruptcy. In the unpublished decision in *Kaiser v. Pappas*, No. 87-C-211-S (W.D. Wis. May 9, 1989) (unpublished opinion), the issue was whether potential spousal rights under the Act constituted a reasonably equivalent value for the transfer of certain stock. The debtor-husband and his wife had entered into a premarital agreement in 1983. The opinion does not set forth or describe the agreement’s provisions. Following the enactment of the Wisconsin Marital Property Act in 1984 but before its effective date, the spouses’ attorney advised them that the Act might have an impact on their agreement when the Act became effective on January 1, 1986. In exchange for one-half the debtor-husband’s stock in a business corporation, in late 1985 the wife agreed to execute a supplement to the premarital agreement unequivocally opting out of the Act and reaffirming the provisions of the 1983 agreement.

After summarily rejecting the argument that marital harmony was sufficient value to support the stock transfer, the U.S. District Court considered whether the potential property rights that might accrue under the Act constituted a reasonably equivalent value that would support the stock transfer for purposes of section 548 of the Bankruptcy Code, 11 U.S.C. § 548 (fraudulent transfers and obligations). The trustee in bankruptcy contended that they did not and sought to recover the transferred stock for the bankrupt husband’s estate.

In dicta, the court spent some time examining section 766.58(12), which purports to preserve marital property agreements entered into before the Act. *See infra* § 7.121 (discussing this provision). The court noted that the meaning of this statute was far from clear and that the 1983 premarital agreement may not have barred a number of rights that might accrue to the wife under the Act, such as (1) marital property rights in the debtor-husband’s earned income, or in income from property titled in his name, and received after the determination date; (2) the right to an elective share in deferred marital property upon the husband’s death; (3) marital property rights that arise through the mixing of marital property with property of other classifications after the determination date; and (4) marital property rights relating to increases in asset value brought about by the uncompensated or undercompensated efforts of either spouse after the determination date.

Assuming for the sake of argument that the foregoing rights arose in the first place, the court concluded that they were all future rights that accrued gradually and did not constitute a presently enforceable right when the transfer of stock to the wife took place in 1985. The court held that the interest in future accretion of property rights through a marital property regime does not constitute a present interest in property. Further, the debtor-husband could exert some control over the accretions, either by terminating the marital relationship or by moving to another jurisdiction. The court viewed the value required by 11 U.S.C. § 548 as limited to the transfer of existing or antecedent property rights or debts. The court held that contingent future rights did not meet the definition.

Although accrual of future marital property rights may not be sufficient consideration or value to prevent the voiding of an asset transfer within the reach of 11 U.S.C. § 548, the surrender of such rights may be adequate and full consideration for transfer tax purposes.

#### **d. Witnesses and Acknowledgment [§ 7.21]**

Neither witnesses nor an acknowledgment before a notary is required for a marital property agreement. However, if the agreement, or a memorandum or affidavit concerning its essential provisions, is to be recorded as a document affecting title to real estate, it must be authenticated or acknowledged and must identify the land to which it relates. Wis. Stat. § 706.05(2). If the marital property agreement is to operate on realty or tangible personal property located in another jurisdiction, the agreement should comply with the other jurisdiction's formal requirements. The laws of other jurisdictions may require acknowledgment or recording. *See* William Q. de Funiak & Michael J. Vaughn, *Principles of Community Property* § 136 (2d ed. 1971); *see also* 2 Alexander Lindey & Louis I. Parley, *Lindey and Parley on Separation Agreements and Antenuptial Contracts* §§ 90.01–.20 (2d ed. 1999 & Supp.).

### 3. Requirements for Amendment or Revocation [§ 7.22]

#### a. In General [§ 7.23]

Generally, a marital property agreement may be amended or revoked only by a later marital property agreement. Wis. Stat. § 766.58(4). There are, however, some exceptions to this rule, as noted below:

1. The statutory terminable marital property classification agreement, *see infra* § 7.175, and the statutory terminable individual property classification agreement, *see infra* § 7.178, specifically authorize one spouse to terminate the agreement at any time by giving signed notice of termination to the other spouse. The termination is effective 30 days after notice is given. Wis. Stat. §§ 766.588(4)(a), .589(4)(a).
2. A nonstatutory marital property agreement may be structured in such a way as to permit termination by the unilateral action of one spouse, as discussed at section 7.117, *infra*; an example appears at section 7.160, *infra*.
3. A will substitute marital property agreement may be amended by a surviving spouse with regard to property subject to the agreement if the agreement provides for the nontestamentary disposition of the property to third persons at the surviving spouse's death, provided that the agreement does not bar the amendment. Wis. Stat. § 766.58(3)(f); *see infra* § 7.101.

The amending or revoking document seemingly must itself comply with the requirements for enforceability of a marital property agreement, including the necessary formalities and minimum disclosures. *See supra* §§ 7.17–.21, *infra* § 7.48. It should be possible to use mutual waivers of disclosure on simple amendments and possibly on revocations if the revocation does not produce a significantly disparate impact on the spouses. Revocations that make the Act applicable to the spouses' property on revocation may require less disclosure.

Presumably, a guardian, acting with the court's prior written approval under section 54.20(2), may execute a marital property agreement that constitutes an amendment or revocation.

➤ **Query.** May spouses amend or revoke a marital property agreement when one or both of the spouses have moved out of Wisconsin? As previously noted, under section 766.58(4) a marital property agreement may only be amended or revoked by a later marital property agreement. Yet under sections 766.03(2) and 766.01(8), the Act applies only while both spouses are married and domiciled in Wisconsin, and unless the Act applies, it is impossible to have a marital property agreement under section 766.58. Thus, in theory, it is impossible for spouses to amend or revoke a Wisconsin marital property agreement once one or both have established a domicile elsewhere. A practical—and reasonable—approach to resolving this dilemma would be for the courts to recognize any amending or revoking document that is signed by both spouses, because it would clearly comply with the spirit of section 766.58(4), even though technically it may not be a marital property agreement.

To summarize, the statutory requirement that both spouses sign a marital property agreement (including an amendment or revocation), *see* Wis. Stat. § 766.58(1), (4), seems to admit of no unilateral right to modify or revoke. However, a mutually agreed-upon actuating provision in a marital property agreement that permits either spouse to terminate the agreement's applicability or to reclassify property subject to the agreement, either prospectively or retroactively, should not run afoul of the prohibition against unilateral amendment and revocation. *See infra* § 7.117.

➤ **Comment.** It is not certain whether the statutory requirement for mutual action applies to documents referred to in a marital property agreement. For example, a will substitute marital property agreement might include provisions purporting to transfer property at a spouse's death to an "outside" trust that is to remain amendable by one spouse alone after the execution of the marital property agreement. Because section 766.58(4) does not address itself to other documents that are referred to in a marital property agreement, the better view is that unilateral amendment of the trust would not violate the statutory requirement.

## **b. Revocation by Operation of Law [§ 7.24]**

Under some limited circumstances, provisions in a marital property agreement are revoked by operation of law. Under section 766.58(3)(f),



provisions for nontestamentary disposition of property at death to the other spouse or third parties under a will substitute marital property agreement are automatically revoked upon dissolution of the marriage, as provided in section 767.375(1). Section 767.375(1) provides that unless a judgment of annulment, divorce, or legal separation provides otherwise, such a judgment revokes a marital property agreement provision providing that

1. Upon the death of either spouse, any of either or both spouses' property, including after-acquired property, passes without probate to a designated person, trust, or other entity by nontestamentary disposition; or
2. One or both of the spouses will make a particular property disposition in a will or other governing instrument, as defined in section 854.01(2). Under section 854.01(2), the term *governing instrument* includes, among other things, wills, deeds, trust instruments, contracts, insurance or annuity policies, retirement plans, beneficiary designations, instruments of nonprobate transfer under chapter 705, and exercises of a power of appointment.

Note that the balance of the marital property agreement between the spouses apparently is not affected by these statutes.

➤ **Comment.** The virtue of section 767.375(1) is that a judgment of dissolution automatically ends *any* provisions in a marital property agreement calling for testamentary or nontestamentary dispositions of property at the death of one or both of the spouses, regardless of whether the transferee or transferees of the property are the other spouses or third parties. In this regard, the statute is similar to but broader than section 854.15, which provides that any provision in a will or other governing instrument executed before an annulment or divorce in favor of the decedent's former spouse or a relative of the former spouse is revoked by the annulment or divorce.

#### **4. Marital Property Agreements Executed Before Marriage [§ 7.25]**

Persons intending to marry may execute a marital property agreement before marriage, but the agreement becomes effective only upon their

marriage. Wis. Stat. § 766.58(5). This provision is consistent with the common law rule that a premarital agreement becomes binding only upon the solemnization of the marriage. *See Hepinstall v. Wixson (In re Hepinstall's Estate)*, 35 N.W.2d 276, 278 (Mich. 1948); *Williams v. Williams*, 569 S.W.2d 867 (Tex. 1978).

## **5. Anticipatory Marital Property Agreements**

### **[§ 7.26]**

Section 766.585 permits spouses or unmarried persons who subsequently marry each other to enter into an anticipatory marital property agreement. This provision also applies to nonresident spouses or spouses-to-be who wish to enter into an anticipatory marital property agreement before establishing their domicile in Wisconsin. Section 766.585(1) states that after April 4, 1984, and before their determination date, such persons may execute a marital property agreement under section 766.58 that is intended to apply only after their determination date to the same extent that persons may execute a marital property agreement after their determination date.

An anticipatory marital property agreement does not apply before the determination date, in contrast to pre-Act marriage agreements intended to be applicable immediately upon execution, *see infra* §§ 7.119–.146. When an anticipatory marital property agreement does become applicable, it has the same effect as if executed after the determination date. The anticipatory marital property agreement provision also makes clear that the law in effect on the date the marital property agreement becomes applicable (i.e., chapter 766)—not the law in effect on the date of its execution—applies to the agreement's execution, enforceability, and other legal effects. Wis. Stat. § 766.585(2).

## **6. Oral Marital Property Agreements [§ 7.27]**

Section 766.58(1) requires that a marital property agreement be a “document,” presumably written, and signed by the parties. Nearly all community property states have statutes requiring that marital agreements be in writing. Some require acknowledgment or recording. *See William A. Reppy, Jr. & Cynthia A. Samuel, Community Property in the United States* 24 (2d ed. 1982).

➤ **Comment.** The potential applicability of the doctrine of partial or full performance to marriage agreements governed by the pre-Act statute of frauds is discussed in section 7.125, *infra*. Unlike section 241.02(1) (which no longer applies to marital property agreements under the Act, *see* Wis. Stat. § 241.02(2)), section 766.58(1) does not state the effect of a failure to comply with the requirement that a marital property agreement be a document. It can be argued that the section 766.58(1) documentation requirements are self-contained and that any agreement that fails to meet them is simply invalid. The other argument is that because the Act does not state whether a purported oral marital property agreement is void or merely unenforceable, it does not go as far as the previous statute of frauds to declare all oral agreements void. Under this view, the requirement of a signed document may be approached somewhat less stringently. There may be circumstances so compelling that a court will be willing to enforce an oral marital property agreement. Consistent with the safeguards for determining whether there has been sufficient performance to take a marriage agreement out of the statute of frauds, *see infra* § 7.125, the equitable doctrine of partial or full performance could be used to enforce an oral marriage agreement that one of the spouses has relied on to his or her substantial detriment. Assuming that those safeguards are applied, the enforcement of a couple's oral agreement through application of the partial or full performance doctrine appears to be consistent with the freedom of choice conferred by the Act. Consistent, too, is the expectation that there will be a much greater need for property agreements between spouses under the Act than was the case before, thus creating more situations in which application of the doctrine may be appropriate.

➤ **Example.** *Hall v. Hall*, 271 Cal. Rptr. 773 (Ct. App. 1990), is illustrative of the above principles. The case arose under the California version of the Uniform Premarital Agreement Act. The specific question posed to the court was whether a substantial change in position in reliance on an oral premarital agreement would take the agreement out of the uniform act's statute-of-frauds requirement that the agreement be in writing and signed by both parties. The court held that the traditional equitable exceptions to the statute of frauds (such as partial or full performance) remained viable under the terms of the uniform act, even though the uniform act did not specifically reference these exceptions. In *Hall*, the wife had quit working, begun taking Social Security early, and advanced substantial funds to her

husband in return for the husband's promise to provide for her financial security in the form of a life estate in his residence if he predeceased her. The court concluded that, because of the wife's expectancy interest arising from her detrimental reliance on the husband's promise, the wife was entitled to specific performance of the agreement.

## **D. Subject Matter of Marital Property Agreements**

### **[§ 7.28]**

#### **1. In General [§ 7.29]**

Section 766.58(3) recognizes a broad range of topics as appropriate subjects for a marital property agreement. Both section 766.58(3)(h) and the comment to UMPA section 10 make clear that the statutory list is not intended to be exclusive. The permissible subjects of a marital property agreement include those enumerated in sections 7.30–.38, *infra*.

#### **2. Property Rights and Obligations [§ 7.30]**

The first subject recognized as appropriate for a marital property agreement is property rights and obligations in the broadest sense of those terms. Included are rights in and obligations with respect to either or both spouses' property "whenever and wherever acquired or located." Wis. Stat. § 766.58(3)(a). This provision is designed to encompass prospective or retroactive classification of property or obligations, including future earnings and acquisitions of property. Classification or reclassification of property by marital property agreement is specifically recognized elsewhere in the Act. *See, e.g.*, Wis. Stat. § 766.31(7)(d), (10).

The term *property* is broadly defined in section 766.01(15) to include present or future interests, legal or equitable interests, and vested or contingent interests in real or personal property. Accordingly, the language in section 766.58(3)(a) should be broad enough to permit reclassification by marital property agreement of assets held in the revocable trust of one or both of the spouses without the necessity of first withdrawing the assets from the trust. The right to revoke alone (and not necessarily any retained beneficial interest) should be treated as

tantamount to outright ownership of individual assets held by the trustee of a revocable trust and should thus permit their reclassification by agreement.

A question may arise when a marital property agreement classifies the spouses' assets as marital property in only general terms and either or both of the spouses own deferred employment benefits or life insurance policies. At issue is the application of

1. The terminable interest rule of section 766.62(5) to deferred employment benefits and to assets in an individual retirement account (IRA) that are traceable to the rollover of deferred employment benefits; and
2. The "frozen interest" valuation rule of section 766.61(7) to the noninsured spouse's property interest in a life insurance policy designating the other spouse as owner and insured.

With regard to the terminable interest rule in section 766.62(5), section 766.58(7)(a) specifically provides that, unless the marital property agreement expressly provides otherwise, a marital property agreement that classifies deferred employment benefits (or assets in an IRA account traceable to a rollover of those benefits) as marital property does not affect (i.e., overrule) the operation of the terminable interest rule. Similarly, with regard to the frozen interest valuation rule in section 766.61(7), section 766.58(7)(b) specifically states that unless the marital property agreement expressly provides otherwise, a marital property agreement that classifies as marital property the noninsured spouse's interest in a policy naming the other spouse as the owner and insured does not affect the operation of the frozen interest rule.

These statutory provisions make clear that if the terminable interest rule in section 766.62(5) or the frozen interest rule in section 766.61(7) are to be negated, they must be negated by specific provisions. For examples of specific language to negate the operation of these statutory rules, see paragraphs I.B. and I.C. of the agreement form at section 7.151, *infra*.

➤ **Note.** It may not be possible to waive by marital property agreement property rights in deferred employment benefits under qualified plans governed by the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. §§ 1001–1461. Deferred

employment benefits are significant components in the wealth of many Wisconsin residents, and recent federal decisions cast doubt on the ability of one spouse (or spouse-to-be) to waive ERISA rights in the other spouse's deferred employment benefits via provisions in a marriage agreement alone, when there is no subsequent postmarriage execution of a formal waiver document meeting the specific requirements of ERISA. The precise issue is whether general waivers of rights contained in a marriage agreement, executed either before or after marriage, operate as an effective written waiver of survivor benefits under the requirements of ERISA, and as reflected in I.R.C. § 417(a)(1) and (2). A developing line of cases tends to indicate that general waivers contained in marriage agreements are not sufficient. See *Hurwitz v. Sher*, 982 F.2d 778 (2d Cir. 1992) (holding that wife-to-be's general waiver of rights in premarital agreement did not operate as effective waiver under I.R.C. § 417(a)(2)(A)); see also *Pedro Enters. v. Perdue*, 998 F.2d 491 (7th Cir. 1993); *Howard v. Branham & Baker Coal Co.*, No. 91-5913, 1992 WL 154571 (6th Cir. July 6, 1992) (unpublished opinion); *Zinn v. Donaldson Co.*, 799 F. Supp. 69 (D. Minn. 1992); *Nellis v. Boeing Co.*, No. 91-1011-K, 1992 WL 122773, at \*5 (D. Kan. May 8, 1992). But see *Brown v. Hopkins (In re Estate of Hopkins)*, 574 N.E.2d 230 (Ill. App. Ct. 1991). Even if the marriage agreement specifically obligates a spouse to execute a waiver meeting the requirements of I.R.C. § 417(a)(2)(A), the courts may still refuse to order the spouse to sign a waiver after the employee spouse's death if the waiver was never presented to the nonemployee spouse for signature before the employee spouse's death. See *Callahan v. Hutsell, Callahan & Buchino, P.S.C.*, 813 F. Supp. 541, 547 (W.D. Ky. 1992), *vacated and remanded without published op.*, 14 F.3d 600 (6th Cir. 1993); see also Lynn Wintriss, *Practice Tips: Waiver of Rights Under the Retirement Equity Act on Premarital Agreements*, 19 ACTEC Notes 82 (1993); *infra* ch. 10.

➤ **Practice Tip.** One possible drafting approach to dealing with the failure of a spouse to waive ERISA survivor benefits as required by a marital property agreement is to offset any qualified plan benefits payable at death to the spouse against any other amounts payable to that spouse under the terms of the agreement. But see *Hisquierdo v. Hisquierdo*, 439 U.S. 572 (1979) (holding, in divorce property-settlement context, that federal preemption with respect to railroad retirement benefits precluded use of offset against other community property).

### 3. Management and Control [§ 7.31]

The second subject recognized as appropriate for a marital property agreement is management and control of the property of either or both of the spouses. *See* Wis. Stat. § 766.58(3)(b); *see also supra* ch. 4 (discussing scope of management and control). A marital property agreement may provide that a nontitled spouse is given the exclusive right to manage and control an asset. This authorization would be binding on third parties having notice of the agreement. In effect, the agreement operates much like a power of attorney, but it is not unilaterally revocable by one spouse unless it specifically so provides.

In addition to providing for management and control of specific assets regardless of ownership, a marital property agreement may also designate the survivorship marital property form of holding marital property assets. *See* Wis. Stat. § 766.58(3)(b), (c). Such a designation should be effective to add a survivorship feature to marital property assets even if the documents of title to the assets are not changed. *See infra* § 7.118.

### 4. Disposition at Dissolution, Death, or Other Event [§ 7.32]

The third subject recognized as appropriate for a marital property agreement is the disposition of any of the property of either or both of the spouses upon the dissolution of the marriage, death, or the occurrence or nonoccurrence of any other event. *See* Wis. Stat. § 766.58(3)(c). Section 766.38(3)(c) allows the spouses to agree that certain property will be transferred into trust at the death of the first spouse to die, or that certain identified assets may be disposed of by a spouse before the death of the first of them, or at the death of either, without regard to the property's classification. Subject to the requirements of sections 767.61(3)(L) and 767.56(8), a marital property agreement may deal with the topics of property division and maintenance in the event of the dissolution of the marriage. *See infra* § 7.107; ch.11.

➤ **Note.** A provision in a marital property agreement requiring a spouse to make a disposition of property upon death or upon the occurrence or nonoccurrence of some event is a contractual undertaking to make a future transfer of property. This is to be

contrasted with using the marital property agreement as a will substitute under section 766.58(3)(f). The latter provision allows the spouses to dispose of assets without probate by nontestamentary means upon the death of either or both of the spouses. *See infra* §§ 7.35, 7.100–106. If a spouse fails to make an agreed-upon disposition by will, trust, beneficiary designation, or other means under section 766.58(3)(c), the failure would give rise to a claim against the deceased spouse’s estate. By contrast, will substitute provisions under section 766.58(3)(f) are directly dispositive and require no collateral documents to carry them out.

## **5. Modification or Elimination of Spousal Support**

### **[§ 7.33]**

The fourth subject recognized as appropriate for a marital property agreement is the modification or elimination of spousal support. *See* Wis. Stat. § 766.58(3)(d). Section 766.58(9) contains two significant exceptions to the general rule that a marital property agreement may modify or eliminate spousal support, which are as follows:

1. Section 766.58(9)(a) provides that a marital property agreement may not result in a spouse’s having “less than necessary and adequate support” during the marriage, taking into consideration all sources of support.
2. Section 766.58(9)(b) provides that a marital property agreement may not render a spouse eligible for public assistance at the time of the dissolution of the marriage or the termination of the marriage by death. If a marital property agreement does render a spouse eligible for public assistance, the court may require the other spouse or the other spouse’s estate to provide the support necessary to avoid that eligibility. Wis. Stat. § 766.58(9)(b).

The first exception, regarding adequate support during the marriage, is not found in UMPA. It is, however, consistent with Wisconsin’s legislative policy, expressed in subsections 49.90(1m), (2), and (4), that spousal maintenance may be compelled.

The second exception, regarding eligibility for public assistance, was taken from UMPA section 10(i), but with a further change—namely, that the eligibility for public assistance may be reviewed at the death of a



spouse as well as at the dissolution of the marriage. This provision is intended to dovetail with the probate court's authority under section 861.35 to provide support to the surviving spouse from the decedent spouse's estate. *See* Wis. Stat. Ann. § 766.58(9)(b) Legis. Council Notes—1985 Act 37, §§ 112–121 (West 2009).

➤ **Comment.** By adding the first exception discussed above and changing the second, the modification of the language of UMPA section 10(i) may diminish the usefulness of marital property agreements in resolving questions of spousal support with complete certainty. The “necessary and adequate” test in section 766.58(9)(a) for support during marriage is not defined. Presumably, this test will be measured by the standards for support and maintenance found in sections 767.501 and 767.56.

➤ **Query.** May the parties to a marital property agreement completely waive the section 861.35 special allowance for the support of a surviving spouse? No guidance is found in section 766.17 or section 766.58. Section 861.35(3)(e) itself indicates that the probate court should consider “whether the provisions of a marital property agreement will create a hardship for the surviving spouse” as one of several factors in making the special allowance under section 861.35. The overriding policy concern in these not entirely harmonious statutory sections seems to be to protect the surviving spouse from the provisions of an otherwise enforceable marital property agreement if it would result in extreme adversity. With that said, complete waivers of support at the death of a spouse should be permissible under section 766.53(3)(d), but the spouses should understand that these may not be enforceable if the waiver renders a surviving spouse eligible for public assistance or otherwise creates a hardship.

## **6. The Making of a Will, Trust, or Other Arrangement [§ 7.34]**

The fifth subject recognized as appropriate for a marital property agreement is the making of a will, trust, or other arrangement to carry out the marital property agreement. *See* Wis. Stat. § 766.58(3)(e). The Act clearly authorizes contractual terms requiring certain provisions in the spouses' testamentary documents, as well as contractual terms requiring transfers of specific property to one spouse or third parties during

lifetime or at death. The Act's presumptions and property ownership rules favoring marital property are likely to necessitate marital property agreements dealing with these subjects whenever the spouses are not content to have most or all of their assets classified as marital property.

➤ **Note.** Provisions under section 766.58(3)(e) for the making of a will, trust, or other arrangement to carry out the marital property agreement are similar to provisions under section 766.58(3)(c) for the disposition of property on dissolution of the marriage, death, or the occurrence or nonoccurrence of some event, *see supra* § 7.32. Both kinds of provisions are executory in nature, requiring future action by one or both of the spouses to accomplish them. They are to be contrasted with will substitute provisions that dispose of assets without probate by nontestamentary means on the death of one or both spouses under section 766.58(3)(f). If a spouse fails to make a will, trust, or other arrangement as required by the marital property agreement, the remedy of the aggrieved spouse is to commence an action against the other spouse or file a claim against the other spouse's estate. By contrast, will substitute provisions under section 766.58(3)(f) are directly dispositive and require no collateral documents or actions to carry them out.

It is possible that joint and contractual wills signed by both spouses, as well as separate agreements between spouses to make wills, may also meet the technical definition of a marital property agreement in subsections 766.58(1), (3)(c), and (3)(e). It is unclear whether future judicial decisions regarding such documents and third-party rights under them will develop independently under section 766.58, or whether the courts will continue to look to section 853.13 and to earlier common-law decisions involving contracts to make wills. *See, e.g., Pederson v. First Nat'l Bank*, 31 Wis. 2d 648, 143 N.W.2d 425 (1966); *Seher v. Kurz (In re Estate of Cochrane)*, 13 Wis. 2d 398, 108 N.W.2d 529 (1961); *Allen v. Ross*, 199 Wis. 162, 225 N.W. 831 (1929); *Doyle v. Fischer*, 183 Wis. 599, 198 N.W. 763 (1924); *cf. Pindel v. Czerniejewski (Estate of Czerniejewski)*, 185 Wis. 2d 892, 592 N.W.2d 702 (Ct. App. 1994); *see also Tweeddale v. Tweeddale*, 116 Wis. 517, 93 N.W. 440 (1903) (discussing agreement to make gifts to third parties on occurrence of certain events).

## 7. Will Substitute Provisions [§ 7.35]

The sixth subject recognized as appropriate for a marital property agreement is the authorization of will substitute provisions—that is, provisions that on the death of either spouse, any property of either or both of the spouses, including after-acquired property, will pass without probate to a designated person, trust, or entity by nontestamentary disposition. Wis. Stat. § 766.58(3)(f). Will substitute marital property agreements of this sort have their genesis in a Washington statute. *See* Wash. Rev. Code § 26.16.120 (West, WESTLAW current with amendments received through January 15, 2010); *see also* UMPA § 10 cmt. Commencing with the effective date of the Act, these agreements created a new estate planning vehicle. *See infra* §§ 7.99–.106 (detailed discussion of will substitute agreements).

## 8. Choice of Law [§ 7.36]

The seventh subject recognized as appropriate for a marital property agreement is choice of the law governing the construction of the agreement. *See* Wis. Stat. § 766.58(3)(g). Note that section 766.58(3)(g) authorizes only choice of the law that will govern construction of the agreement, not choice of the law that will govern its validity or enforceability. Careful drafting ordinarily dictates use of a choice-of-law clause that is intended to govern validity and enforceability as well as construction. Perhaps the courts will deem validity and enforceability to be covered by the catchall provision, section 766.58(3)(h), discussed in section 7.37, *infra*.

May spouses, only one of whom is domiciled in Wisconsin, choose the law of a single state—that is, either the law of Wisconsin or the law of the other state—to govern their property rights and the construction of a marital property agreement? Neither section 766.58(3)(g) nor any other part of section 766.58 expressly deals with the choice of a domicile. In part, this may reflect the fact that domicile depends not only on intention but also on physical presence, the latter of which an agreement clearly cannot confer.

In any event, it is an open question whether dual-domicile spouses may elect to have the Act's provisions apply to their marriage. Under sections 766.01(8) (defining *during marriage*) and 766.03 (applicability of the Act), the Act applies only during periods in which *both* spouses

are domiciled in Wisconsin. If the Act does not apply, neither does the statutory section dealing with marital property agreements, section 766.58, including its choice-of-law provision, section 766.58(3)(g).

Section 766.03(1) does recognize some exceptions to the general rule that the Act applies only while both spouses are domiciled in Wisconsin. The statute references section 766.58(5) (permitting persons intending to marry to enter into a marital property agreement that becomes effective upon their marriage); section 766.58(12) (providing that provisions in a document signed before the determination date by spouses or by unmarried persons who subsequently marry that affect the property of either of them and is enforceable by either without reference to chapter 766, are not affected by chapter 766); and section 766.585 (permitting spouses or unmarried persons who subsequently marry to execute a marital property agreement under section 766.58 that is intended to apply only after their determination date).

Thus, if the parties (at least one of whom is not domiciled in Wisconsin) execute a marriage agreement in Wisconsin that seeks to apply the property regime described in the Act and indicates that Wisconsin law is to govern the validity and construction of the agreement, two results are possible. If the agreement is intended to apply only after the determination date, section 766.585(1) indicates that the agreement *cannot* apply before the determination date. A determination date will not occur as long as one of the spouses continues to be domiciled outside of Wisconsin, and thus the choice-of-law provision in section 766.58(3)(g) would remain in suspense. On the other hand, if the agreement is intended to apply in whole or in part before the determination date, section 766.585(3) indicates that the agreement is governed by section 766.58(12), which in turn provides that the agreement is enforceable by either of the parties without reference to chapter 766 and is not affected by chapter 766 except as provided otherwise in a marital property agreement made after the determination date. This is likely to throw the court back to an analysis of the Wisconsin law applicable to marriage agreements before the Act, *see infra* §§ 7.122–.146, or the law with respect to marriage agreements that has since developed independent of the Act. In view of the above, it appears doubtful that parties to a marital property agreement will be able to adopt a Wisconsin marital property regime unless both parties are domiciled in Wisconsin.

Note that a consensual community property regime based on contract alone and without the force of state law would not be accorded the income tax benefits that flow to a legal system of community property.

## **9. Other Matters Affecting Property [§ 7.37]**

The final subject appropriate for a marital property agreement covers any other matter that affects the property of either or both of the spouses and does not violate public policy or a statute imposing a criminal penalty. *See* Wis. Stat. § 766.58(3)(h). Section 766.58(3)(h) is derived from and is substantially identical to UMPA section 10(c)(8). For reasons that are not clear, the UMPA provision is not as broad as section 3(a)(8) of the Uniform Premarital Agreement Act, 9B U.L.A. 373 (1983) [hereinafter Uniform Premarital Agreement Act], which permits the spouses to contract with respect to “any other matter, *including their personal rights and obligations*, not in violation of public policy or a statute imposing a criminal penalty,” without limiting the matters to those affecting property (emphasis added).

Section 766.58(3)(h) was cited by the court of appeals in *State v. Wing*, No. 91-0362-CR, 1991 WL 285874 (Wis. Ct. App. Nov. 7, 1991) (unpublished opinion not citable per section 809.23(3)), in holding invalid on public policy grounds a marital property agreement, the application of which would have resulted in a spouse’s circumventing the indigency requirements for public-expense legal representation of criminal defendants under section 977.07.

## **10. Noneconomic Matters [§ 7.38]**

Section 766.58 purports to deal only with property and economic considerations. No special mention is made of the kinds of personal rights or obligations that the parties sometimes might wish to include in a marriage agreement. Among these might be the spouses’ responsibilities for child rearing, housework, religious matters, and the like. It can be argued that the failure of section 766.58(3) to mention personal rights and obligations implies that they are not a permissible subject in a marital property agreement. On the other hand, it can also be argued that, based on the broad contractual freedom conferred by section 766.17, these contractual provisions will be enforced to the extent that they are enforceable under otherwise applicable law. *See Avitzur v.*

*Avitzur*, 446 N.E.2d 136 (N.Y. 1983) (holding that provisions in agreement requiring arbitration of religious obligations before specified rabbinical panel were enforceable as “secular terms,” even though agreement was entered into as part of religious ceremony); *Schwarzman v. Schwarzman*, 388 N.Y.S.2d 993, 998 (Sup. Ct. 1976) (stating that provisions in valid premarital agreement regarding religious upbringing of children are enforceable if in child’s best interests).

One commentator has advanced several reasons to explain why noneconomic provisions in marriage agreements are not appropriate subjects for judicial enforcement:

Where the antenuptial contract purports to regulate aspects of the marriage other than support or finances, the foregoing objections to judicial enforcement [i.e., judicial economy and avoidance of increased legal regulation of the marriage relationship] apply with equal force. The few cases which have arisen in the past have refused to enforce agreements to obtain a divorce, agreements not to defend a divorce action, agreements respecting sexual relations between the spouses, and in one unusual case the agreement that the children of the wife’s prior marriage would not live with the parties. Most such cases rest on the traditional view that the incidents of marriage are established by law and may not be altered by the parties. This of course is not a reason but merely another way of stating the result, and it is somewhat inconsistent with the courts’ contemporary willingness to permit control of alimony and maintenance by antenuptial agreement. Nevertheless, the results of these cases may be justified as saving the time and energies of the courts and as taking the realistic position that the intimate day to day conduct of married persons cannot be controlled by judicial decision, whether or not the decision is based upon the parties’ own contract.

Homer H. Clark, Jr., *Antenuptial Contracts*, 50 U. Colo. L. Rev. 141, 163 (1979) (footnotes omitted). On the other hand, this commentator recognized that marriage agreements dealing with noneconomic issues may be useful as a means of revealing the expectations of (and thus possible conflicts between) persons contemplating marriage. *Id.*

➤ **Practice Tip.** Because section 766.58(3) is silent on the permissibility of including noneconomic matters in a marital property agreement, and because the enforceability of noneconomic provisions is open to some doubt, it may be desirable to deal with noneconomic matters in a separate document.

## E. Enforceability of Marital Property Agreements [§ 7.39]

### 1. In General [§ 7.40]

Regardless of whether executed before or during marriage, a marital property agreement under the Act is enforceable at any time

1. If the agreement was not unconscionable when made;
2. If it was voluntarily executed; and
3. If, before or at the time of execution of the agreement, the spouse received fair and reasonable disclosure, under the circumstances, of the other spouse's property and financial obligations, or had notice of the other spouse's property and financial obligations.

*See Wis. Stat. § 766.58(6).* Stated another way, the agreement will fail if the spouse against whom enforcement is sought proves *any one* of the following: unconscionability when the agreement was made; involuntary execution; or inadequate disclosure and lack of notice. The burden of proof is on the spouse seeking to avoid the agreement. *Id.* Neither *unconscionability* nor *fair and reasonable disclosure under the circumstances* is defined in the Act. As yet, there are no court decisions involving UMPA in Wisconsin or elsewhere to provide guidance, other than decisions involving related uniform acts, *see infra* § 7.43, or commercial law analogies, *see infra* § 7.44. Moreover, the persuasiveness of decisions involving pre-Act agreements, *see infra* §§ 7.122–.131, in the context of marital property agreements under the Act remains unknown. For a discussion of the categories and attributes of pre-Act marriage agreements, see section 7.120, *infra*.

Apart from the Act's requirements, if the marital property agreement is to be enforceable as an arrangement for property division in the event of dissolution, there is an additional requirement that it must be equitable as to both parties. Wis. Stat. § 767.61(3)(L); *see infra* §§ 7.133–.140. For a comparison with the common law standards of enforceability of marriage agreements, see sections 7.122–.131, *infra*.

It should be noted that the enforceability provisions contained in section 766.58(6) differ significantly from the provisions of UMPA

section 10. UMPA provides two standards for the enforceability of marital property agreements. One, contained in section 10(f), governs the enforceability of marital property agreements executed during marriage. The other, contained in section 10(g), governs the enforceability of marital property agreements executed before marriage and is based on section 6 of the Uniform Premarital Agreement Act. Assuming that a marital property agreement was voluntarily executed, the enforceability tests contained in UMPA subsections 10(f) and (g) differ in one key respect. Under UMPA section 10(g), a premarital agreement is enforceable unless it is shown *both* that it was unconscionable when made *and* that there was no fair and reasonable disclosure, no waiver of disclosure, or no notice of the other spouse's property and financial obligations. Under the UMPA section 10(f) standard for postmarital agreements, *either* unconscionability *or* inadequate disclosure alone is a ground for avoiding the agreement.

Section 766.58(6) adopted the UMPA section 10(f) *postmarital* agreement standard as the sole test for enforceability of *both* premarital and postmarital agreements but added certain changes discussed in section 7.48, *infra*. These changes preclude a complete waiver of disclosure in many instances. The result is that under the Act, either unconscionability or inadequate disclosure is a ground for avoidance of a voluntarily executed premarital or postmarital agreement. Thus, avoidance of premarital agreements is made easier under the Wisconsin statute than it would be under UMPA section 10. For a comparison of the enforceability standards under the Act, UMPA, and the Uniform Premarital Agreement Act, see June Miller Weisberger, *Spousal Property Agreements: An Evolving Concept in Wisconsin and Elsewhere*, 5 Wis. Women's L.J. 43, 69–76 (1990).

## **2. Unconscionability [§ 7.41]**

### **a. In General [§ 7.42]**

The requirement that a marital property agreement not be unconscionable when made is somewhat analogous to the fairness test for marriage agreements under pre-Act common law, although the fairness test also includes fraud and duress. *See infra* § 7.128. The statute specifies that unconscionability is an issue to be decided by the court as a matter of law. Wis. Stat. § 766.58(8). The apparent meaning of this provision is that unconscionability is not to be treated as a



question of fact to be submitted to a jury for resolution but rather is reserved to the court for determination after consideration of the relevant facts.

There is tension between the unconscionability standard of section 766.58(6)(a) and the equitableness standard found in the divorce property division statute, section 767.61(3)(L). Section 766.58(6)(a) renders a marital property agreement unenforceable if it was “unconscionable when made.” Section 767.61(3)(L), on the other hand, has been interpreted to permit the court to refuse to enforce the agreement as a vehicle for property division at the dissolution of the marriage if, through significantly changed circumstances, it is “inequitable as to either party” at the time of dissolution, even though it might have been conscionable (i.e., fair and reasonable) when made. *See Button v. Button*, 131 Wis. 2d 84, 388 N.W.2d 546 (1986); *cf. Schumacher v. Schumacher*, 131 Wis. 2d 332, 388 N.W.2d 912 (1986); *see also infra* §§ 7.133–.140. Accordingly, it can be said that the enforceability standards of section 766.58(6) apply with certainty only at the death of one of the spouses or in an enforcement proceeding during the ongoing marriage. The unconscionability portion of the statutory test appears to be replaced by the equitableness standard of section 767.61(3)(L) at dissolution. Neither the courts nor the legislature has attempted to harmonize the two statutes. *See infra* § 7.107.

Although they have not done so yet, it is likely that the appellate courts will be called on to determine what constitutes unconscionability for purposes of section 766.58(6)(a). Resolution of this issue will not be free of difficulty. Like pornography, unconscionability is difficult for the courts to define, but “they know it when they see it.” Stated another way, the determination tends to be subjective.

## **b. Under Uniform Acts [§ 7.43]**

The unconscionability test embodied in section 766.58(6)(a) is contained in UMPA section 10(f) and emanates from a series of uniform acts. The first is the Uniform Premarital Agreement Act. Section 6 of the Uniform Premarital Agreement Act provides that unconscionability is one element for avoiding premarital agreements. As discussed in section 7.40, *supra*, UMPA section 10(g) included the substance of section 6 of the Uniform Premarital Agreement Act, but these provisions were not included in section 766.58(6).

The comment to Uniform Premarital Agreement Act section 6 quotes extensively from the Commissioners' Note to Uniform Marriage and Divorce Act section 306. The latter is particularly instructive because it discusses the early antecedents of the test for unconscionability in the commercial context and interprets their application to marital relations. The relevant portion of the comment in the Uniform Premarital Agreement Act states

The following discussion set forth in the Commissioners' Note to section 306 of the [Uniform Marriage and Divorce Act] is equally appropriate here:

"Subsection (b) undergirds the freedom allowed the parties by making clear that the terms of the agreement respecting maintenance and property disposition are binding upon the court unless those terms are found to be unconscionable. The standard of unconscionability is used in commercial law where its meaning includes protection against one-sidedness, oppression, or unfair surprise (see section 2-302, Uniform Commercial Code), and in contract law, *Scott v. U.S.*, 12 Wall (U.S.) 443 (1870) ('contract . . . unreasonable and unconscionable but not void for fraud'); *Stiefler v. McCullough*, 174 N.E. 823, 97 Ind. App. 123 (1931); *Terre Haute Cooperage v. Branscome*, 35 So. 2d 537, 203 Miss. 493 (1948); *Carter v. Boone County Trust Co.*, 92 S.W.2d 647, 338 Mo. 629 (1936). It has been used in cases respecting divorce settlements or awards. *Bell v. Bell*, 371 P.2d 773, 150 Colo. 174 (1962) ('this division of property is manifestly unfair, inequitable and unconscionable'). Hence the act does not introduce a novel standard unknown to the law. In the context of negotiations between spouses as to financial incidents of their marriage, the standard includes protection against overreaching, concealment of assets, and sharp dealing not consistent with the obligations of marital partners to deal fairly with each other.

"In order to determine whether the agreement is unconscionable, the court may look to the economic circumstances of the parties resulting from the agreement and any other relevant evidence, such as the conditions under which the agreement was made, including the knowledge of the other party."

Section 306 of the Uniform Marriage and Divorce Act authorizes the parties to a marriage to enter into a written separation agreement attendant on their separation or the dissolution of their marriage. Section 306(b) further provides that the terms of the separation agreement (with certain limited exceptions) are binding on the court unless the court finds that the separation agreement is unconscionable. In this respect, the statute is analogous to section 767.255(3)(L), except that the uniform act test is stated in terms of unconscionability rather than inequity.

Illinois (along with seven other states) has adopted the substance of the Uniform Marriage and Divorce Act, 750 Ill. Comp. Stat. Ann. 5/101 to 5/802 (West, WESTLAW current through P.A. 96-891 of the 2010 Reg. Sess.), and its decisions on the enforcement of separation agreements are therefore instructive in ascertaining the scope of unconscionability. The Illinois Appellate Court has held that if an agreement is unreasonably favorable to one party and the circumstances surrounding execution indicate that the other party did not have a meaningful choice, the agreement may be held to be unconscionable. *See In re Marriage of Richardson*, 606 N.E.2d 56, 65 (Ill. App. Ct. 1992); *In re Marriage of Carlson*, 428 N.E.2d 1005, 1010–11 (Ill. App. Ct. 1981); *cf. In re Marriage of Van Zuidam*, 516 N.E.2d 331, 333–34 (Ill. App. Ct. 1987) (stating that agreement is not unconscionable if it is negotiated over several months, both parties were represented by counsel, agreement is not overly one-sided, and there are no allegations of fraud). Additional considerations include whether the agreement was the result of duress, fraud, misrepresentation, or concealment of assets at the time of execution, and whether the agreement was one-sided or oppressive considering the parties' economic circumstances. *See In re Marriage of Tabassum*, 881 N.E.2d 396 (Ill. App. Ct. 2007) (appeal denied); *In re Marriage of Smith*, 518 N.E.2d 450 (Ill. App. Ct. 1987); *In re Marriage of Miller*, 424 N.E.2d 1342 (Ill. App. Ct. 1981). The Illinois Appellate Court decisions make clear that something more than mere unfairness is necessary to invalidate an agreement. *In re Marriage of Lorton*, 561 N.E.2d 156, 160 (Ill. App. Ct. 1990); *In re Marriage of Van Zuidam*, 516 N.E.2d 331, 334 (Ill. App. Ct. 1987); *In re Marriage of Kloster*, 469 N.E.2d 381 (Ill. App. Ct. 1984). The Illinois Appellate Court has also stated that traditional commercial law concepts of unconscionability must be applied to determine whether the economic results of a separation agreement are unconscionable. *In re Marriage of Foster*, 451 N.E.2d 915, 918–19 (Ill. App. Ct. 1983).

A Missouri decision under the Uniform Marriage and Divorce Act stated that unconscionability was “inequality so strong, gross, and manifest that it must be impossible to state it to one with common sense without producing an exclamation at the inequality of it.” *Peirick v. Peirick*, 641 S.W.2d 195, 197 (Mo. Ct. App. 1982). However, in another case arising under the Uniform Marriage and Divorce Act, a Kentucky court held that a separation agreement will not be held unconscionable solely on the basis that it is a bad bargain. *See Peterson v. Peterson*, 583 S.W.2d 707, 712 (Ky. Ct. App. 1979).

Two cases cited in the comment to Uniform Premarital Agreement Act section 6 also assist in fleshing out the concept of unconscionability applicable to marriage agreements (as opposed to separation agreements). In *Ferry v. Ferry*, 586 S.W.2d 782 (Mo. Ct. App. 1979), the court struck down a premarital agreement waiving support and property division because (1) it appeared that one of the parties was operating under an erroneous assumption when the agreement was entered (namely, that the agreement was necessary to protect the anticipated inheritance of her child by a prior marriage); (2) that party did not have independent counsel, was given only limited time to review the agreement, and did not receive an accurate disclosure of assets; and (3) the agreement was unreasonably favorable to the other party. The court noted that “[c]onscionability is the same standard employed in commercial law, meaning protection against onesidedness, oppression or unfair surprise.” *Id.* at 786.

In the second case, *Newman v. Newman*, 653 P.2d 728 (Colo. 1982), the court determined that portions of a premarital agreement that waived maintenance on the dissolution of the marriage were not unconscionable when the affected spouse had reasonable means of self-support at the time of dissolution. The court declined to apply an unconscionability standard to the agreement’s property division provisions, observing that such agreements are subject to a fairness review at divorce “within the common law context of review for fraud, overreaching, or sharp dealing.” *Id.* at 733. According to the court, the analysis takes place at the time of execution of the contract and not at the time of separation. (The rule in Wisconsin for agreements intended to be enforceable at dissolution is different. *See infra* § 7.107.) Thus, despite a considerable disparity of monetary consideration, the agreement in *Newman* was upheld because the spouse against whom enforcement was sought was aware of the other spouse’s wealth when the agreement was made and had decided not to obtain independent counsel. Compare *Newman* with *In re Marriage of Meisner*, 715 P.2d 1273 (Colo. Ct. App. 1985), in which the court cited *Newman* for the proposition that a premarital agreement barring maintenance will be found unconscionable if the spouse seeking maintenance is left without means of reasonable support, either because of a lack of property or a condition of unemployability.

In adopting its version of the Uniform Premarital Agreement Act, New Jersey added a statutory definition of unconscionability. An unconscionable premarital agreement is an agreement that, as a result of a party’s lack of property or unemployability, would

1. Render a spouse without a means of reasonable support;
2. Make a spouse a public charge; or
3. Provide a standard of living far below that which was enjoyed before the marriage.

N.J. Stat. Ann. § 37:2-32 (West, WESTLAW current with laws effective through L.2010, c. 6). While not intended to be all-inclusive, this statutory definition at least covers the most egregious situations. Note, however, that the definition does not require that dire changes in economic circumstances be the result of overreaching, concealment, sharp dealing, or borderline fraud.

### **c. Wisconsin Commercial Law Analogies [§ 7.44]**

The discussion and citations in section 7.43, *supra*, relating to various uniform acts, form a backdrop for a review of other Wisconsin statutes and cases that contain standards for finding unconscionability in contracts. For example, the Wisconsin Consumer Act, Wis. Stat. chs. 421–427, contains a statutory list of factors bearing on the issue of unconscionability. See Wis. Stat. § 425.107. Cases decided under this statute, as well as those decided under section 402.302 of the Uniform Commercial Code, may be useful in defining unconscionability for purposes of section 766.58(6)(a).

In *Discount Fabric House v. Wisconsin Telephone Co.*, 117 Wis. 2d 587, 345 N.W.2d 417 (1984), the Wisconsin Supreme Court, quoting extensively from *Allen v. Michigan Bell Telephone Co.*, 171 N.W.2d 689, 692–94 (Mich. Ct. App. 1969), divided the determination of unconscionability into the following two questions: (1) What are the parties' relative bargaining power, economic strength, and sources of supply—in a word, their options? and, (2) is the challenged term substantively reasonable? *Discount Fabric House*, 117 Wis. 2d at 601. The court cited *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445 (D.C. Cir. 1965), for the proposition that unconscionability has generally been recognized to include an absence of meaningful choice on the part of one of the parties, together with contract terms that are unreasonably favorable to the other party. *Discount Fabric House*, 117 Wis. 2d at 601. The court refers to James J. White and Robert J. Summers, *Uniform Commercial Code* (1972), for an explanation of the procedural and

substantive aspects of unconscionability. *Procedural unconscionability* consists of absence of meaningful choice, superiority of bargaining power, unfair surprise, sharp practices, or deception. *Substantive unconscionability* consists of unfair terms (including overall imbalance), an unfair price, or an unfair disclaimer of a legal obligation. White and Summers explain that courts have had difficulty defining unconscionability because it is not a concept but a determination. Therefore, rather than trying to define the term, courts should be concerned with citing factors to be considered in determining whether a contract is unconscionable. See, e.g., Wis. Stat. § 425.107; see also *Leasefirst v. Hartford Rexall Drugs, Inc.*, 168 Wis. 2d 83, 483 N.W.2d 585 (Ct. App. 1992); *Pietroske, Inc. v. Globalcom, Inc.*, 2004 WI App 142, 275 Wis. 2d 444, 685 N.W.2d 884.

Within the context of family relationships, courts have indicated a willingness to apply stricter scrutiny to transactions, requiring good faith and conscientious dealing. See *Bogie v. Bogie*, 41 Wis. 209 (1876). The affectionate and trusting atmosphere that pertains in a contract between parent and child also exists in contracts between husband and wife or persons who are engaged to be married, with similar legal consequences. See, e.g., *Newman*, 653 P.2d at 732; see also *Button*, 131 Wis. 2d at 95. The self-interest assumed to be present in the commercial context may not be assumed in the marital context.

Courts in other jurisdictions that have reviewed marriage agreements for unconscionability have been somewhat inconsistent in formulating standards for defining the term. It is not clear whether Wisconsin courts will (1) limit unconscionability to the middle ground between an unequal (but not necessarily unfair) bargain, on the one hand, and various species of active misrepresentation and fraud, on the other; or (2) include fraud and misrepresentation in the term's definition along with overreaching, gross inequality, and unfair advantage. The answer is likely to emerge from future judicial decisions interpreting the Act.

#### **d. Effect of Not Retaining Separate Counsel** **[§ 7.45]**

When legal counsel is retained in connection with a marital property agreement, the fact that both parties are represented by one counsel, or that one party is represented by counsel and the other party is not represented, does not by itself render the agreement unconscionable or

unenforceable. Wis. Stat. § 766.58(8). This provision is clearly intended to cover the situation in which both spouses are willing to use the services of a single attorney or firm to prepare a marital property agreement, as well as the situation in which one of the spouses is represented by an attorney, and the other prefers neither to be represented by that attorney nor to retain any other. The clarifying amendments to section 766.58(8) adopted by the 1985 Trailer Bill deleted a requirement that made this provision conditional on each spouse waiving independent representation in writing, because in practice the requirement might have proved to be a trap for the unwary if the written waiver were overlooked or omitted.

If dual representation by itself is not a determinative factor bearing on the unconscionability of a marital property agreement, it may become one when considered in conjunction with other factors tending to show unconscionability. These might include gross disparity of benefits under the agreement, inadequate disclosure, and lack of time to review the agreement before execution. For further discussion of the question of independent representation, see section 7.128, *infra*.

➤ **Practice Tip.** An attorney preparing a marital property agreement for both spouses must carefully consider potential conflicts of interest under the Rules of Professional Conduct for Attorneys. See *infra* ch. 14. The 1985 Trailer Bill Supplemental Nontax Note to section 766.58(8) makes clear that the statutory language is not intended to address the ethical considerations required of a lawyer under the Rules of Professional Conduct for Attorneys in situations of this sort. See Wis. Stat. Ann. § 766.58 Legis. Council Comm. Supplemental Notes Relating to 1985 Act 37 (West 2009).

#### **e. Effect of Not Making Provision for Spouse** **[§ 7.46]**

It should be possible for a party to a marital property agreement—a party represented by counsel, in possession of a fair and reasonable disclosure of the other party’s property and financial obligations, and not acting under duress or with inadequate time to consider the matter—to voluntarily choose to take no property from his or her spouse. Neither the Act nor its legislative history contains any hint that it is necessary to make some financial provision for a spouse in a marital property

agreement to ensure that the agreement will not be unconscionable. The absence of financial provisions is not uncommon in marital property agreements executed before marriage by spouses-to-be, each of whom has significant personal assets. This is particularly true of marriages occurring later in life. Cases such as *Newman*, 653 P.2d 728, indicate that such agreements should not be deemed unconscionable.

### 3. Voluntary Execution [§ 7.47]

The requirement of voluntary execution contained in section 766.58(6)(b) is analogous to the common law requirement that marriage agreements be free from duress. *See infra* §§ 7.55, .128.

However, voluntary execution may involve more than the mere absence of duress. In *In re Marriage of Matson*, 730 P.2d 668, 671 (Wash. 1986), the Washington Supreme Court listed the following factors as possibly indicative of involuntariness: “The bargaining positions of the parties, sophistication of the parties, presence of independent advice, understanding of the legal consequences and rights, and timing of the agreement juxtaposed with the wedding date.” Although one of these factors alone may not be sufficient to invalidate a marital property agreement, the conjunction of several may well do so. *See also Bonds v. Bonds*, 5 P.3d 815 (Cal. 2000), for an extensive discussion of the requirements for voluntary execution under the California version of section 6 of the Uniform Premarital Agreement Act. In *Bonds*, the court cited the importance of evidence of coercion or lack of knowledge, including such factors as the proximity of the execution of the agreement to the wedding; a surprise in the presentation of the agreement; the presence or absence of independent counsel or of an opportunity to consult with independent counsel; inequality of bargaining power, in some cases indicated by the relative ages and sophistication of the parties; whether there was full disclosure of assets; and the parties’ understanding of the rights being waived under the agreement, or at least their awareness of the intent of the agreement. *Id.* at 824–25.

With regard to independent advice, a crucial issue seems to be not so much whether the spouse claiming invalidity actually consulted with counsel but rather whether that spouse had the *reasonable opportunity* to obtain independent counsel. *See, e.g., Greenwald v. Greenwald*, 154 Wis. 2d 767, 782–83, 454 N.W.2d 34 (Ct. App. 1990) (finding premarital



agreement voluntarily executed in situation in which husband's attorney advised wife to retain independent counsel to review agreement, but wife rejected advice and signed agreement); *see also* *Woolwine v. Woolwine*, 519 So. 2d 1347 (Ala. Civ. App. 1987).

On the other side of the coin are cases in which the spouse asserting invalidity had no reasonable opportunity to obtain counsel. In that situation, the agreement is at risk of being considered involuntary. *Norris v. Norris*, 419 A.2d 982 (D.C. 1980) (noting that, when husband first proposed premarital agreement several weeks before marriage, wife initially consulted with attorney and refused to sign premarital agreement, but husband later asked wife to execute agreement one hour before ceremony); *Lutgert v. Lutgert*, 338 So. 2d 1111 (Fla. Dist. Ct. App. 1976) (noting that agreement was presented to wife on day before wedding, and wife had no opportunity to consult with independent counsel); *Zimmie v. Zimmie*, 464 N.E.2d 142 (Ohio 1984) (noting that wife first learned of agreement one day before wedding); *In re Estate of Crawford*, 730 P.2d 675 (Wash. 1986) (noting that wife first learned of agreement at husband's attorney's office three days before wedding); *Matson*, 730 P.2d 668 (noting that agreement was first presented four days before wedding by attorney representing both husband and wife, and attorney did not explain legal significance of wife's waiver of community property rights). One party's threats or interference in connection with the other party's efforts to secure independent counsel normally will invalidate a premarital agreement. *See Casto v. Casto*, 508 So. 2d 330 (Fla. 1987); *Sogg v. Nevada State Bank*, 832 P.2d 781 (Nev. 1992).

Several of these issues arose in *In re Marriage of Foran*, 834 P.2d 1081 (Wash. Ct. App. 1992). In this case the court held that, under Washington law, if a premarital agreement is economically unfair, the party seeking enforcement of the agreement will be required to prove that each party entered into the agreement both voluntarily *and* intelligently. The court concluded that the wife, who was not represented by counsel and who was seriously disadvantaged by the agreement in an economic sense, had not entered into it voluntarily and intelligently, because the evidence indicated that she had not fully understood the agreement's legal and economic consequences. Facts influencing this conclusion included the following: (1) the husband's lawyer prepared the agreement and the wife first saw it a day before she and the husband left on a trip to be married; (2) the husband had physically abused the wife before the marriage; (3) the husband's

attorney had informed the wife that he represented only the husband and recommended that she seek independent counsel but did not explain why it was important that she do so; and (4) the wife likely did not have adequate time to review the agreement.

Under Wisconsin law, the same result perhaps would be reached under an analysis of duress or undue influence, *see infra* §§ 7.55, .56, rather than that of “intelligent” execution. This follows from the fact that section 766.58(6)(b) requires only voluntary execution for enforceability of a marital property agreement. For further discussion of the difficult position of the lawyer under these circumstances, see chapter 14, *infra*.

Nonetheless, a premarital agreement presented for execution only a short time before the wedding date might be held valid if there is evidence that the parties had informally discussed it or negotiated its terms before a draft of the agreement was prepared and presented. *See In re Marriage of Byrne*, 535 N.E.2d 14 (Ill. App. Ct. 1989) (noting that desirability of agreement was discussed by parties; agreement was then drafted by wife’s attorney at her request, and signed by parties several days before wedding without wife again consulting with her attorney); *In re Marriage of Adams*, 729 P.2d 1151 (Kan. 1986) (noting occurrence of informal discussions for a week, including consultation with attorney; draft of agreement was presented for execution one hour before marriage); *Howell v. Landry*, 386 S.E.2d 610 (N.C. Ct. App. 1989) (informal discussion for one month preceding wedding; draft agreement presented one day before wedding, and party claiming invalidity negotiated last-minute changes); *In re Marriage of Leathers*, 779 P.2d 619 (Or. Ct. App. 1989) (noting that agreement was discussed in general terms for “extended period of time” before wedding; formal document presented evening before wedding); *Williams v. Williams*, 720 S.W.2d 246 (Tex. App. 1986) (noting that informal discussions took place six months before marriage; agreement was presented one day before marriage); *Hengel v. Hengel*, 122 Wis. 2d 737, 365 N.W.2d 16 (Ct. App. 1985) (noting that agreement was signed by wife after husband threatened to postpone wedding plans; wife had received draft agreement weeks before wedding, consulted with her lawyer, negotiated a change, and knew “many months” before wedding that husband would not remarry without an agreement); *see also Hill v. Hill*, 356 N.W.2d 49 (Minn. Ct. App. 1984). Cases upholding an agreement are often difficult to distinguish on their facts from cases invalidating the agreement, indicating that the issue of voluntariness is fact-sensitive and subject to case-by-case analysis.

However, even if the disadvantaged party presented with a marital property agreement shortly before the wedding date is able to consult with counsel, there is no guarantee that counsel will have adequate time to give meaningful advice. *See Orgler v. Orgler*, 568 A.2d 67 (N.J. Super. Ct. App. Div. 1989). *But see DeLorean v. DeLorean*, 511 A.2d 1257 (N.J. Super. Ct. Ch. Div. 1986) (holding that in a case in which a disadvantaged party consulted counsel hours before wedding and signed agreement despite counsel's recommendation that agreement not be executed, agreement was not necessarily rendered invalid). See also the discussion of an attorney's ethical responsibilities under these circumstances in chapter 14, *infra*.

#### **4. Disclosure [§ 7.48]**

Just as disclosure is an important element in the validity of pre-Act marriage agreements, it is also critical to the enforceability of marital property agreements under the Act. (Pre-Act marriage agreements are discussed generally in section 7.120, *infra*, and disclosure in such agreements is discussed in section 7.126, *infra*.) Under section 766.58(6)(c), a marital property agreement is not enforceable if the spouse seeking to avoid the agreement can prove that the following two conditions existed at or before the execution of the agreement:

1. He or she did not receive fair and reasonable disclosure under the circumstances of the other spouse's property or financial obligations; and
2. He or she did not have notice of the other spouse's property or financial obligations.

*Notice* is a defined term under the Act. A person has notice of a fact if he or she has knowledge of it, receives a notification of it, or has reason to know that it exists from the facts and circumstances known to him or her. Wis. Stat. § 766.01(13).

The two-part disclosure test in section 766.58(6)(c) represents a considerable change from UMPA section 10(f)(3), which specifically recognizes that a spouse's waiver of disclosure (beyond those disclosures actually provided) also meets the test. The clear implication in the change from the UMPA language is that a waiver of disclosure—at least a blanket waiver of disclosure—is not allowed.

The 1985 Trailer Bill Original Nontax Note to section 766.58(6)(c) comments that although it might have been desirable to legislatively establish a minimum-disclosure requirement, it would have been difficult to formulate the requirement so that it would not have been excessive under some circumstances. Accordingly, the disclosure required for an enforceable marital property agreement under the Act depends on the circumstances of each case; it is possible that under some circumstances no disclosure will be required for an enforceable agreement. *See* Wis. Stat. Ann. § 766.58 Legis. Council Notes—1985 Act 37, §§ 112—121 (West 2009). For example, nondisclosure is expected to pass muster in the case of limited marital property agreements, *see infra* §§ 7.116, .155—.157, when the assets being classified or the obligations being assumed represent a relatively small part of the spouses' overall economic picture, or when the spouses have knowledge (or reason to know) of each other's property and financial obligations when the agreement is entered into. Similarly, an agreement opting into the Act is likely to require less disclosure than one opting out. In most cases, the absence of disclosure (coupled with a lack of notice about the other spouse's assets or financial obligations) will result in the agreement's not being enforced if it is attacked by the party against whom enforcement is sought. *See supra* § 7.40.

Any discussion of minimum-disclosure requirements must give consideration to *Schumacher*, 131 Wis. 2d 332, which involved the enforceability of a pre-Act marriage agreement at divorce. The spouses in *Schumacher* had entered into a premarital agreement in which the wife-to-be waived any rights in specifically enumerated assets constituting approximately 88% of the husband-to-be's total net worth. The agreement did not purport to affect the parties' other assets. These other assets were not disclosed in the agreement or contemporaneously with its execution. The court noted that while de minimis omissions alone would not vitiate the agreement, the parties here did not make a sufficient disclosure of their assets to each other to constitute fair and reasonable disclosure for purposes of *Button*, 131 Wis. 2d 84, discussed in sections 7.107 and .135—.138, *infra*. In addition, although the parties apparently had some independent knowledge of each other's finances, the court singled out their failure to exchange lists of assets and liabilities as being at the heart of their failure to make fair and reasonable disclosure.

Although the case did not involve a marital property agreement under the Act, there is language in *Estate of Campbell v. Chaney*, 169 Wis. 2d

399, 485 N.W.2d 421 (Ct. App. 1992), to the effect that if an attorney drafts a premarital agreement without “attaching a financial statement,” a fact-finder might conclude that the attorney failed to use reasonable care. This might be true even if the agreement was later enforced because, for example, the spouse against whom enforcement was sought had prior knowledge of the financial information. *Id.* at 410.

Presumably, *Chaney* will not apply to marital property agreements under the Act because neither section 766.58(6)(c) nor any Wisconsin appellate decision interpreting it requires physical attachment of financial disclosures as a prerequisite to enforceability of a marital property agreement. Moreover, the statute places the burden of establishing unenforceability on the spouse against whom enforcement is sought: he or she must establish affirmatively that, before execution of the agreement, he or she did not receive fair and reasonable disclosure, under the circumstances, of the other spouse’s property or financial obligations, and that he or she did not have notice (i.e., actual knowledge) of the other spouse’s property or financial obligations. Wis. Stat. § 766.58(6)(c).

Under the Act, it appears permissible to disclose assets and liabilities by general groupings or categories. The financial disclosure statements that are part of the statutory terminable property classification agreements, *see infra* §§ 7.175, .178, specifically contemplate disclosure in that fashion.

The statutory disclosure requirements may make self-drafted “kitchen table” marital property agreements lacking financial disclosures unenforceable, particularly when one spouse does not have notice of the other spouse’s assets or obligations and gives up substantial rights. The steps necessary to comply with the statutory “fair and reasonable ... under the circumstances” disclosure requirements are not likely to be well understood by laypersons.

Sample memoranda of assets, liabilities, and income that are intended to meet the fair and reasonable disclosure requirements are set forth in sections 7.169 and .172, *infra*.

## 5. Other Contract Defenses [§ 7.49]

### a. In General [§ 7.50]

The three reasons listed in section 766.58(6) for avoidance of a marital property agreement (unconscionability, involuntariness, inadequate disclosure), *see supra* §§ 7.41–.48, are not intended to be exclusive. The comment to UMPA § 10 indicates that ordinary contract defenses (other than lack of consideration) are also available.

At common law, contracts can be policed from three perspectives: the contract's substance, the parties' status, and the parties' behavior. Courts are generally reluctant to permit a party to avoid a contract based on the substance of its terms for three reasons: (1) courts are ill-equipped to prescribe fair contractual terms; (2) they want to encourage certainty in contract law; and (3) they are reluctant to interfere with freedom of contract. *See* 1 E. Allan Farnsworth, *Farnsworth on Contracts* § 4.1 (4th ed. 2004). However, it should be noted that marriage agreements between spouses, particularly those intended to be enforceable at dissolution, are at least partial exceptions to this general rule. *See Button*, 131 Wis. 2d 84 (noting that equity is “competing public policy” in divorce cases); *see also infra* § 7.133–.140.

### b. Incapacity [§ 7.51]

The doctrine of incapacity allows contracts to be avoided based on the parties' status. There are two standards for finding incapacity, one definite and the other uncertain.

The definite basis for finding incapacity is age: contracts made by parties under the legal age to contract are void or voidable unless they are for the purchase of necessities. *Halbman v. Lemke*, 99 Wis. 2d 241, 245, 298 N.W.2d 562 (1980); *see also Madison Gen. Hosp. v. Haack*, 124 Wis. 2d 398, 402–04, 369 N.W.2d 663 (1985). Parties are able to contract at the age of majority (i.e., at age 18) in Wisconsin.

The uncertain basis for finding incapacity is mental infirmity. There are two tests for determining mental capacity: first, whether the party has cognitive understanding of the transaction's nature and consequences (the other party's knowledge of the mental infirmity is irrelevant); and

second, given that the party can understand the transaction, whether he or she is unable to control his or her behavior. Under this second, or volitional, test, the afflicted party can avoid a contract if the other party has knowledge of this inability. Restatement (Second) of Contracts § 15 (1981); *Hauer v. Union State Bank*, 192 Wis. 2d 576, 532 N.W.2d 456 (Ct. App. 1995); *see also Guardianship of Hayes*, 8 Wis. 2d 32, 39, 98 N.W.2d 430 (1959). Intoxicated persons or persons under the influence of drugs are found incapacitated according to this test if the other party has reason to know of the intoxication or drug use. 1 Farnsworth, *supra* § 7.50, § 4.6 at 438.

Therefore, marital property agreements can be avoided if one of the contracting parties (1) is under age 18, (2) lacks cognitive understanding of the transaction's nature and consequences, or (3) can understand the transaction but cannot control his or her behavior and the other party has knowledge of this inability. A marital property agreement voluntarily entered into by an intoxicated person or a person under the influence of drugs, for example, is voidable if the other party had reason to know of the condition.

### **c. Misrepresentation, Duress, and Undue Influence [§ 7.52]**

#### **(1) In General [§ 7.53]**

Courts will permit a contract to be avoided because of the behavior of one of the contracting parties if that party abuses the bargaining process by engaging in misleading or coercive conduct. To protect the integrity of a contract system based on informed consent, courts rely on the doctrines of misrepresentation, duress, and undue influence. 1 Farnsworth, *supra* § 7.50, § 4.9.

#### **(2) Misrepresentation [§ 7.54]**

Generally, misrepresentation consists of the following four elements: (1) an assertion was made that was not in accord with the facts; (2) the assertion was either fraudulent or material; (3) the assertion was relied on regarding assent; and (4) the reliance was justified. Restatement (Second)

of Contracts § 164 (1981); *see also id.* §§ 161(d), 162; 1 Farnsworth, *supra* § 7.50, §§ 4.10–.14.

The Wisconsin common law definition of fraudulent misrepresentation consists of three, not four, elements. Those elements are as follows:

1. There must be a statement of fact that is untrue.
2. The false statement must be made with intent to defraud and for the purpose of inducing the other party to act on it.
3. The other party must rely on the false statement and must be induced thereby to act to his or her injury or damage.

*Merten v. Nathan*, 108 Wis. 2d 205, 209 n.2, 321 N.W.2d 173 (1982). There are no Wisconsin decisions specifically involving marriage agreements.

### **(3) Duress [§ 7.55]**

Generally, duress is coercive conduct, including physical compulsion or threat. Restatement (Second) of Contracts § 175 cmt. a (1981). Wisconsin has adopted the modern view of duress, which holds that contracts and transfers may be voided “when procured by business or economic compulsion, as well as by physical coercion.” *Mendelson v. Blatz Brewing Co.*, 9 Wis. 2d 487, 494, 101 N.W.2d 805 (1960). Although all contracts involve an implicit threat (e.g., pay what I demand or go without), the courts have established a four-element test for determining what threats reach the status of duress: (1) a threat, (2) that is improper, (3) manifestation of assent, and (4) that is sufficiently grave to justify the assent. 1 Farnsworth, *supra* § 7.50, §§ 4.16–.18; *see also* Restatement (Second) of Contracts § 176 (1981).

The Act incorporates the doctrine of duress by making voluntary execution a requirement for an enforceable marital property agreement. *See* Wis. Stat. § 766.58(6)(b). The issue of duress is most likely to arise in marital property agreement cases because of the implicit threat in the premarital context to “sign the agreement or I won’t marry you” and in the postmarital context to “sign the agreement or I will divorce you.”



The threat not to marry a person, however, is unlikely to be considered sufficiently grave to justify assent. This threat does not deprive the other person of his or her free will without a reasonable alternative; that is, the other not only is not compelled to go through with the marriage but also is free to marry someone else. Indeed, persons entering a second marriage often do so with the mutual understanding that having a premarital agreement is a condition of their marriage, and failure to work out the terms of an agreement will cause the parties to go their own ways. *See, e.g., Hengel v. Hengel*, 122 Wis. 2d 737, 365 N.W.2d 16 (Ct. App. 1985).

On the other hand, a premarital agreement presented for the first time on the eve or day of the wedding, accompanied by a threat not to go through with the marriage unless the agreement is signed, may not be regarded as freely and voluntarily entered into, *see Lutgert v. Lutgert*, 338 So. 2d 1111 (Fla. Dist. Ct. App. 1976), although a contrary conclusion was reached in *DeLorean*, 511 A.2d 1257.

In *DeLorean*, the husband-to-be presented the wife-to-be with a marriage agreement a few hours before the ceremony and threatened to cancel the marriage if the wife did not sign. The court concluded that although cancelling the wedding might have been embarrassing for the bride-to-be, she was not compelled to go through with the ceremony and therefore had not executed the agreement under duress. 511 A.2d at 1259. *Accord Howell v. Landry*, 386 S.E.2d at 617 (holding that shortness of time between presentation of premarital agreement and date of wedding is insufficient alone to permit finding of duress).

When one party conditions the marriage on execution of a premarital agreement, that fact will not invalidate an agreement. *See Greenwald v. Greenwald*, 154 Wis. 2d 767, 454 N.W.2d 34 (Ct. App. 1990); *see also Walters v. Walters*, 580 So. 2d 1352, 1354 (Ala. 1991); *Liebelt v. Liebelt*, 801 P.2d 52, 55 (Idaho Ct. App. 1990); *Rose v. Rose*, 526 N.E.2d 231 (Ind. Ct. App. 1988). The courts usually give the reason that the threat of a refusal to marry is not wrongful in the eyes of the law and therefore not duress. *Liebelt*, 801 P.2d at 55; *Rowland v. Rowland*, 599 N.E.2d 315, 329 & n.3 (Ohio Ct. App. 1991) (Stephenson, P.J., dissenting).

The courts are divided on whether a threatened refusal to marry a pregnant woman unless she executes a premarital agreement constitutes duress. The courts in *Hamilton v. Hamilton*, 591 A.2d 720 (Pa. Super. Ct. 1991) (noting that woman had been represented by counsel at time of

executing agreement), and *Bassler v. Bassler*, 593 A.2d 82 (Vt. 1991), suggested that there was no duress under these circumstances; in *Williams v. Williams*, 617 So. 2d 1032 (Ala. 1992), and *Rowland*, the courts held that pregnancy, coupled with other factors surrounding the execution of an agreement, may add up to duress.

A postmarital agreement, presented by one spouse to the other with the statement that it is in contemplation of divorce, should not by itself be considered a threat of sufficient gravity to constitute duress, particularly if the other spouse has adequate time to consider the agreement and is able to consult with independent counsel. Most states have no-fault divorce statutes; virtually all states provide for maintenance and equitable property division in the event of divorce. Accordingly, the implicit or explicit threat of divorce is unlikely to render the spouse receiving it powerless. However, the threat of divorce coupled with threats to deprive a spouse of support, custody of children, or property clearly risks being treated as duress. Such conduct could be deemed an economic or personal compulsion sufficiently grave to vitiate a postmarital agreement. See, e.g., *Baltins v. Baltins*, 260 Cal. Rptr. 403 (Ct. App. 1989); *Eckstein v. Eckstein*, 379 A.2d 757 (Md. Ct. Spec. App. 1978); see also Restatement (Second) of Contracts §§ 175, 176 (1981).

#### **(4) Undue Influence [§ 7.56]**

The typical case of undue influence consists of a victim whose weakness does not quite constitute incapacity and a perpetrator whose improper persuasion does not quite constitute misrepresentation or duress. According to the Restatement (Second) of Contracts § 177 (1981), a claim of undue influence has two elements: (1) a special relationship between the parties, and (2) an improper persuasion of the weaker party by the stronger party. At issue is whether the result was caused by means that seriously impaired the weaker party's free and competent exercise of judgment. Factors considered include imbalance of result, unavailability of independent advice, lack of time for reflection, and susceptibility to influence. 1 Farnsworth, *supra* § 7.50, § 4.20.

The element of a special relationship between the parties is certainly satisfied by marriage and is probably satisfied by an engagement to marry. Although there are no Wisconsin cases defining the special relationship in the context of marriage, a Colorado decision has held that the relationship of spouses and of persons engaged to marry is one of

confidence and trust in which the weaker party may be justified in assuming that the stronger will not act inconsistently with the welfare of the weaker. *Newman v. Newman*, 653 P.2d 728 (Colo. 1982). The element of improper persuasion is met if methods used by the dominant party seriously impair the weaker party's free and competent exercise of judgment.

Wisconsin has adopted a somewhat more complex four-pronged test for determining whether undue influence has occurred in the contractual context. The Wisconsin Supreme Court has held that to prove undue influence, a plaintiff must establish "susceptibility, opportunity to influence, disposition to influence and coveted result." *Onderdonk v. Keepman (In re Estate of Taylor)*, 81 Wis. 2d 687, 699, 260 N.W.2d 803 (1978). In addition, undue influence must be established by clear, satisfactory, and convincing evidence. *Id.*

#### **d. Contrary to Public Policy [§ 7.57]**

Contracts may be unenforceable as being contrary to public policy. Agreements between spouses governing property settlements or support in the event of the dissolution of the marriage were once held unenforceable as being contrary to a public policy against impairment of family relationships, but more recently courts have permitted considerable freedom of contract in this area. 2 Farnsworth, *supra* § 7.50, § 5.4, at 48. In Wisconsin, this change has been accomplished by statute, *see infra* §§ 7.133–140, and is subject to further public-policy standards relating to child support and spousal support contained in the Act. *See* Wis. Stat. § 766.58(2), (9).

#### **e. Mistake; Impracticability of Performance [§ 7.58]**

Several related judicial doctrines exist to deal with situations in which a basic assumption in a contract fails. These include the doctrines of mistake and of impracticability of performance.

### **(1) Mistake [§ 7.59]**

A contract may be unenforceable because of mutual or unilateral mistake. A *mistake* is defined as a belief that is not in accord with the facts that exist when the contract is made. Restatement (Second) of Contracts § 151 (1981).

To establish a defense of *mutual mistake*, the party must show that (1) a mistake occurred with regard to a basic assumption on which the contract was made—for example, the existence, identity, quality, and quantity of the subject matter; (2) the mistake has a material effect on the exchange of performances so severe that the party cannot fairly be required to perform; and (3) the mistake is not one with respect to which the party bears the risk. *Id.* § 152. The risk is borne by the party who is assigned the risk by the agreement, who is consciously ignorant after deciding not to pursue the answer, or who has been allocated the risk by the court as reasonable under the circumstances.

To establish a claim of *unilateral mistake*, a party must establish the same conditions required for mutual mistake, and in addition must prove either that enforcement of the contract would create unconscionable hardship or that the other party knew or had reason to know of the first party's mistake. *Id.* § 153; 2 Farnsworth, *supra* § 7.50, § 9.3; *see also In re Marriage of Agustsson*, 585 N.E.2d 207 (Ill. App. Ct. 1992); *Ferry v. Ferry*, 586 S.W.2d 782 (Mo. Ct. App. 1979) (discussed at section 7.43, *supra*).

### **(2) Impracticability of Performance [§ 7.60]**

A contract may be voidable because of impracticability of performance. Restatement (Second) of Contracts § 261 (1981). Circumstances may change to such a degree that enforcement of the contract would be inequitable. A party must show that the changed circumstances concern a basic assumption on which the contract was made and that they occurred without negligence or willful action on his or her part. The court may deem the changed circumstances a contingency intended by the parties but not incorporated into the contract. In deciding whether or not to reform the contract, the courts will examine questions such as the following: Was the contingency unforeseeable? Was a remedial clause easy to insert into the contract? *See* 2 Farnsworth, *supra* § 7.50, § 9.6.

In the context of marital property agreements, impracticability could result from

1. Unanticipated loss or destruction of the property that was the subject matter of the agreement;
2. Significant deterioration in the health of one of the spouses;
3. The substantial disability of one of the spouses;
4. Substantial changes in employability of one of the spouses;
5. The birth of a child, particularly an unplanned pregnancy occurring to a middle-aged couple with grown children from prior marriages;
6. A dramatic decline in the spouses' living standard; or
7. A spouse's other profoundly changed circumstances.

The doctrine of unforeseeable change of circumstances appears to be a component in determining the equitableness (and thus the enforceability) of marriage agreements at divorce in Wisconsin and other jurisdictions. *Button*, 131 Wis. 2d 84, established the proposition that an agreement that was fair at the time of its execution may be unfair to the parties at the time of divorce if, as the result of significantly changed circumstances, it no longer comports with the parties' reasonable expectations. *Id.* at 98–99. The Wisconsin Supreme Court has indicated that this is a test of reasonable foreseeability, one that requires the parties to an agreement to consider both the circumstances existing at the execution of the agreement and those that are reasonably foreseeable. *Id.* at 97. Other states have used a similar test when faced with the issue of enforceability of marriage agreements at divorce. *See, e.g., McHugh v. McHugh*, 436 A.2d 8 (Conn. 1980).

In *Warren v. Warren*, 147 Wis. 2d 704, 433 N.W.2d 295 (Ct. App. 1988), the Wisconsin Court of Appeals applied these principles to uphold a premarital agreement. In *Warren*, it was shown that an event not specifically covered by the terms of the premarital agreement—namely, the early retirement of one of the spouses—nonetheless had been discussed during the negotiations. The spouse in question in fact took early retirement shortly after the agreement was signed and before the

marriage. With reference to the reasonable foreseeability test, the court stated:

The idea behind the test is that both spouses have a right to rely upon the prenuptial agreement when all subsequent events transpire as logically anticipated.

The premarital agreement is, after all, a contract with all of its attendant risks and risk bearing. Risk may be defined as uncertainty in regard to cost, loss, or damage. A. Kronman & R. Posner, *The Economics of Contract Law* 26 (1979). A person signing a premarital agreement undertakes all the normal anticipated risks that the agreement may not prove to be a wise one. Only when a future event can be said to have been too uncertain can it be said that the risk assumed is out of proportion to the loss incurred.

*Id.* at 710–11. Because the parties to the agreement in *Warren* not only foresaw the eventuality that one of the parties would take early retirement but also discussed it when the agreement was being negotiated, the spouse's early retirement was not viewed as an unforeseen changed circumstance that would justify disregarding the agreement.

Courts in jurisdictions that have considered the question have shown no inclination to permit avoidance of marriage agreements at death because of the substantially changed circumstances of one of the spouses, assuming that other requirements for enforceability of the agreement are met. *See infra* §§ 7.122–.131.

## **6. Statutes of Limitation [§ 7.61]**

### **a. In General [§ 7.62]**

The general statute of limitation for actions based on contract requires that the action be commenced within six years after the cause of action accrues. Wis. Stat. § 893.43. Additionally, there are specific statute-of-limitation provisions that apply to some aspects of marital property agreements. *See* Wis. Stat. § 766.58(13).

## **b. Actions to Enforce Provisions Effective at Death or Dissolution [§ 7.63]**

Under section 766.58(13)(a), any statute of limitation applicable to an action to enforce a provision of a marital property agreement that is effective on or after the dissolution of the marriage or the termination of the marriage by death is tolled until dissolution or death, respectively. Chapter 893, dealing generally with statutes of limitation, cross-references to this provision. *See* Wis. Stat. § 893.135. Presumably, actions to enforce provisions in a marital property agreement requiring performance during marriage may be brought within the normal six-year contract statute of limitation.

The 1985 Trailer Bill Original Nontax Note to section 766.58(13) states the reason for the tolling of any applicable statutes of limitation as follows:

[I]n order to avoid the potentially disruptive effect of compelling litigation between spouses during marriage in order to escape the running of any applicable statute of limitations, any applicable limitations period should be tolled during the marriage of the parties to a marital property agreement with regard to provisions of the agreement that are effective upon or after dissolution or termination of the marriage.

Wis. Stat. Ann. § 766.58 Legis. Council Notes—1985 Act 37, §§ 112 to 121 (West 2009). The 1985 Trailer Bill Original Nontax Note to section 766.58(13) also points out that equitable defenses limiting the time for enforcement, such as laches and estoppel, are still available to either party. *Id.* The note includes the observation that the tolling provision is based on section 8 of the Uniform Premarital Agreement Act but is not as broad in scope.

Because actions relating to the enforceability of arrangements for contractual property settlement typically arise shortly following the death of one spouse or the commencement of an action for dissolution, the section 766.58(13)(a) tolling provision in most cases should cause little hardship. Virtually all the Wisconsin cases dealing with the validity and enforceability of pre-Act marriage agreements (discussed in sections 7.119–.147, *infra*) arose either after the death of one of the parties to the agreement or during divorce proceedings involving the parties. *See infra* §§ 7.123–.131, .134–.140. If a difficulty lies in the tolling of the statute of limitation, it is most clearly presented when the marriage terminates

by death, since one of the parties to the marital property agreement is no longer available to be heard in its defense. Obviously, this problem does not exist when the marriage is ended by dissolution unless one of the spouses is incompetent.

### **c. Actions Commenced After Spouse's Death** **[§ 7.64]**

Section 766.58(13)(b) contains a special limitation period for commencement of actions concerning a marital property agreement after a spouse's death. It provides that no such action may be brought later than six months after the inventory is filed in the estate under section 858.01. If an amended inventory is filed, the action may be brought within six months after the filing of the amended inventory if the action relates to information contained in the amended inventory that was omitted in a previous inventory. Wis. Stat. § 766.58(13)(b). The court may extend the six-month period for cause if a motion for extension is made within the original applicable six-month period. Wis. Stat. § 766.58(13)(c).

➤ **Comment.** Section 766.58(13) does not adequately deal with the common situation in which the estate is informally administered under chapter 865 and no inventory is filed. *See* Wis. Stat. § 865.11(2). Nor does it deal with situations in which the estate is summarily settled using one of the procedures in chapter 867.

Sections 766.58(13), 859.01, and 859.02 dovetail to address the situation in which a surviving spouse must file a claim against the deceased spouse's estate to enforce financial provisions in a marital property agreement because the provisions have not been carried out by the decedent. *See infra* ch. 12. As a general proposition, section 859.01 permits the probate court by order to set a deadline for filing a claim against the decedent's estate. The deadline may be no less than three nor more than four months from the date of the order. Wis. Stat. § 859.01. With certain exceptions, all claims against the decedent's estate, whether absolute or contingent, liquidated or unliquidated, are barred unless filed on or before the deadline for filing claims. Wis. Stat. § 859.02(1). Among the few classes of claims that are not subject to the bar of section 859.02(1) are those based on a marital property agreement that are subject to the special time limitations under subsection 766.58(13)(b) or



(c). Wis. Stat. § 859.02(2)(a). Section 859.02(2)(a) eliminates any uncertainty about the interplay between (1) the six-month limitation period in section 766.58(13)(b) and (c) for commencing actions with respect to a marital property agreement and (2) the three-to-four-month period in sections 859.01 and 859.02(1) for filing claims. The Legislative Council Note to section 859.02 indicates that the more generous six-month time period of subsection 766.58(13)(b) or (c) is to apply. *See* Wis. Stat. Ann. § 859.02 Legis. Council Notes—1991 Act 301, § 34 (West 2002).

#### **d. Actions Commenced After Dissolution** **[§ 7.65]**

No special period of limitation similar to section 766.58(13)(b) is prescribed for commencing an enforcement action concerning a provision in a marital property agreement when the marriage terminates by dissolution. If the action to enforce a provision in such an agreement falls within the usual statute of limitation governing actions on contracts, section 893.43, it must be commenced within six years after the cause of action accrues. Because of the tolling provision in section 766.58(13)(a), the six-year period may begin running at dissolution, that is, at the date of the judgment of divorce, annulment, or legal separation. Does this mean that a dissatisfied spouse can bring a separate action for enforcement of the marital property agreement provision and thereby collaterally attack a judgment that rejected the provision in the division of the spouses' property? The statute may produce an unintended result in this situation. This would appear to be an anomalous result.

Perhaps all issues relating to the enforceability of a marital property agreement should be required to be litigated in the dissolution proceedings under chapter 767 and should be deemed to be resolved by the judgment of dissolution. Failure to raise the question of enforceability of the marital property agreement provision in the action for dissolution should bar its pursuit in a subsequent separate action based on section 766.58(13)(a). Such a rule would not preclude a former spouse from later seeking to reopen a divorce property division judgment on appropriate equitable grounds. *Compare* Wis. Stat. § 767.59(1c)(b) (providing that portions of judgment with respect to final division of property are not subject to revision or modification), *with Conrad v. Conrad*, 92 Wis. 2d 407, 284 N.W.2d 674 (1979) (holding that divorce judgment may be reopened within one year concerning property division

under subsection 806.07(1)(a) or (c) for reason of mistake, inadvertence, surprise, excusable neglect, fraud, misrepresentation, or other misconduct, or within a “reasonable time” for other reasons justifying relief under section 806.07(1)). *See also Thorpe v. Thorpe*, 123 Wis. 2d 424, 367 N.W.2d 233 (Ct. App. 1985) (holding that postjudgment change in federal law regarding military pensions provided basis for exercise of court’s discretion under section 806.07 in modifying property division). *But see Winkler v. Winkler*, 2005 WI App 100, 282 Wis. 2d 746, 699 N.W.2d 652 (holding that postjudgment change in public employer’s policy permitting former husband to receive enhanced retirement benefits did not warrant reopening property division pursuant to section 806.07).

## **7. Miscellaneous Considerations [§ 7.66]**

### **a. In General [§ 7.67]**

Two other statutory provisions not contained in UMPA bear indirectly on the enforceability of marital property agreements and thus merit comment. *See infra* §§ 7.68–.69.

### **b. Arbitration [§ 7.68]**

Spouses may enter into an enforceable written agreement to arbitrate controversies arising under chapter 766 or under a marital property agreement. Wis. Stat. § 766.58(10). An agreement to this effect is enforceable under the arbitration provisions of chapter 788. *Id.*

There are a number of policy reasons for arbitrating domestic disputes, including disputes arising under marital property agreements. Arbitration is a voluntary contract entered into by parties for the purpose of securing a final disposition of a controversy between them in an expeditious, inexpensive, and perhaps less formal manner than litigation. *DeLorean*, 511 A.2d at 1263. Arbitration reduces the duration and cost of the adjudication process. It enables the parties to choose their own judge and gives them the opportunity to resolve the dispute in a private forum in which the decision will not become a matter of public record, absent a request for judicial review. *Id.*

However, arbitration has significant disadvantages. First, the arbitrator is not bound by the usual rules of evidence and may not be as

knowledgeable about the substantive law at issue as a trial judge. Second, there is limited room for judicial review. *Id.*; *see, e.g.*, Wis. Stat. § 788.10; *Nicolet High Sch. Dist. v. Nicolet Educ. Ass'n*, 118 Wis. 2d 707, 348 N.W.2d 175 (1984). Third, questions may arise as to the interplay between an arbitration clause and a spouse's right to pursue interspousal remedies under section 766.70. Drafting an arbitration clause to affirm or negate specific subject matter areas or remedies may prove both difficult and expensive. These factors may lead a party to conclude that he or she would obtain a better result in a court of law.

### **c. Recordation [§ 7.69]**

Section 766.58(11) provides that a marital property agreement may be recorded with the county register of deeds. No substantive benefits flow from recording; in fact, section 766.56(2)(a) specifically states that recording does not constitute actual or constructive notice to third parties for purposes of credit transactions. Recording may, however, establish the existence and genuineness of a marital property agreement in some circumstances, and possibly the classification of certain assets on the date of the agreement. Recording is also necessary if the agreement or its essential elements are to be made part of a chain of title to real estate. *See supra* § 7.21. Recording an agreement may prove cumbersome; because recording makes the agreement a matter of public record, any subsequent amendment or revocation to the agreement may have to be recorded to clear the public record.

## **8. Enforceability in Part: Severability or Divisibility [§ 7.70]**

One of the issues confronting the drafter of a marital property agreement containing (1) novel provisions, (2) provisions relating to noneconomic matters, *see supra* § 7.38, or (3) provisions intended to be enforceable in the event of the dissolution of the marriage, *see infra* § 7.107, is the desirability of enforcing the remaining portions of the agreement if one or another of the special provisions is found to be impracticable, unenforceable, or invalid. For example, a provision or group of provisions may be so central to the agreement from the perspective of one of the parties that a failure of that provision would cause the party to want the entire agreement to fail. On the other hand, the failure of one or more provisions that the parties do not regard as

being at the heart of their bargain may not adversely affect their desire to see the balance of the agreement enforced. *See* 2 Farnsworth, *supra* § 7.50, § 5.8.

The Wisconsin Supreme Court has listed a number of ways in which the question of divisibility may arise:

(1) as to the sufficiency of a consideration on the one side to support two or more covenants on the other; (2) in connection with the effect of an illegal covenant upon the remaining valid covenants in the contract; (3) in connection with the statute of frauds upon a contract some of whose covenants are within the scope of the statute; (4) in connection with an attempt to [dis]affirm part of a voidable contract and to ratify the rest; (5) in connection with questions of performance, in cases in which certain covenants have been performed substantially and others have not; (6) in connection with the effect of a judgment upon certain covenants as merging the remaining covenants of the contract.

*Fuller v. Ringling*, 186 Wis. 470, 474, 202 N.W. 183 (1925).

If the concept of divisibility is to be applied, two requirements normally must be met. First, the parties' performances must be capable of being apportioned into corresponding pairs of part performances, and second, it must be appropriate to regard the parts of each pair as agreed equivalents. 2 Farnsworth, *supra* § 7.50, § 5.8, at 81, § 8.13, at 475; Restatement (Second) of Contracts § 240 (1981).

If a part of an agreement offends public policy, the courts may impose two additional requirements: (1) the impropriety must not affect the entire agreement, *see Schara v. Thiede*, 58 Wis. 2d 489, 206 N.W.2d 129 (1973); and (2) the party seeking enforcement must not have engaged in serious misconduct, *see Simenstad v. Hagen*, 22 Wis. 2d 653, 126 N.W.2d 529 (1964). 2 Farnsworth, *supra* § 7.50, § 5.8 at 81–82. Usually, the courts will be more inclined to enforce part of a divisible contract in favor of a party who has already relied on the agreement through preparation or performance. The dilemma facing a court confronted with the issue of whether a contract is divisible, and therefore enforceable in part, is well stated by Farnsworth:

If the party against whom enforcement is sought is the party who desired the inclusion of the [unlawful] term, the court may face a difficult choice between holding the entire agreement unenforceable and holding the agreement enforceable with the exception of the offensive term. Though

refusing to enforce the entire agreement may seem extreme if the offensive part is relatively small, enforcing the agreement without the term against the party who sought its inclusion will deprive that party of part of the expected performance, with no concession in return. However, if this part of the performance is not a material part of the agreed exchange, a court will often enforce the rest of the agreement in favor of a claimant who did not engage in serious misconduct.

*Id.* at 82; *see also* Restatement (Second) of Contracts § 184 (1981).

The drafting of workable severability clauses in marital property agreements poses considerable difficulty. If a broad severability provision such as that found at paragraph [VIII.][IX.]H. of the sample agreement at § 7.154, *infra*, is used in a marital property agreement containing property settlement provisions that become effective at the dissolution of the marriage, the court's refusal to enforce all or part of those provisions at the time of dissolution may cause one of the parties to conclude that not enforcing the entire agreement would be preferable. On the other hand, the court's refusal to enforce a comparatively minor feature of the agreement may still leave the parties wanting the balance of the agreement enforced. A hybrid approach to severability may be possible under these circumstances. For example, the parties might identify certain provisions in the marital property agreement as being so essential that if any one of them were not enforced, they would prefer to see the entire agreement rendered unenforceable. These provisions might be set out as exceptions to the broad severability language mentioned above.

## **F. Statutory Property Classification Agreements**

### **[§ 7.71]**

#### **1. In General [§ 7.72]**

In response to concerns about the need for simple statutory forms to render the Act either inapplicable or fully applicable to spouses' property, the legislature has adopted three statutory marital property agreement forms. Two of these statutory agreements were enacted as part of the 1988 Trailer Bill and are currently available for use. These are the statutory terminable individual property classification agreement in section 766.589 and the statutory terminable marital property classification agreement in section 766.588. *See infra* §§ 7.73–.82, .83–

92. The third kind of statutory agreement, the statutory individual property classification agreement in section 766.587, was a creation of the 1985 Trailer Bill and was effective only between January 1 and December 31, 1986. All such agreements automatically terminated on January 1, 1987, and were not renewable. *See infra* §§ 7.93–.98.

## **2. Statutory Terminable Individual Property Classification Agreements [§ 7.73]**

### **a. In General [§ 7.74]**

Section 766.589 provides for statutory terminable individual property classification agreements (STIPCAs). A STIPCA's operative effect depends on whether the parties complete a financial disclosure form prescribed in the STIPCA form, *see* Wis. Stat. § 766.589(10). If the financial disclosure is completed, a STIPCA applies until ended by the dissolution of the marriage, the death of a spouse, unilateral termination by one spouse, or bilateral termination by both. Wis. Stat. § 766.589(3)(c). If the disclosure is not completed, a STIPCA terminates automatically three years after the date of execution, unless ended earlier by unilateral or bilateral action of the spouses. Wis. Stat. § 766.589(3)(b). The STIPCA form is reproduced at section 7.178, *infra*. Without disclosure, a STIPCA may be a satisfactory device to enable spouses moving into Wisconsin for reasons of employment to avoid the application of Wisconsin's marital property laws for up to three years. With disclosure, a STIPCA may prove to be a relatively simple device for classifying the spouses' property for estate planning and probate purposes when the spouses are both represented by one attorney. Regardless of whether disclosure occurs, a STIPCA may be terminated by the unilateral action of either spouse.

A STIPCA must be identical to the language included in the statutory form. *See* Wis. Stat. § 766.589(2), (10). No variation is permitted. However, the statute explicitly states that section 766.589 is not the exclusive means by which the spouses may reclassify their marital property. Wis. Stat. § 766.589(8). Nonstatutory marital property agreements, declarations of gift, conveyances, consents, and unilateral statements are all alternative methods of reclassifying property. *See* Wis. Stat. § 766.31(10); *see also supra* ch. 2.

## **b. Property Law Consequences [§ 7.75]**

Under section 766.589(1)(b), execution of a STIPCA classifies the spouses' presently owned marital property, and property acquired, reclassified, or created in the future that would otherwise be marital property, as the owner's individual property. For purposes of determining ownership of property classified by a STIPCA, a spouse "owns" property if the property is "held" by that spouse. Wis. Stat. § 766.589(1)(a). See also the discussion of the concept of holding in chapter 4, *supra*. If property classified by a STIPCA is not held by either or both of the spouses, ownership of the property is determined as if the spouses were unmarried when the property was acquired. Wis. Stat. § 766.589(1)(a). The importance of this reclassification arrangement is somewhat diminished, however, because the reclassification does not prevent the deferred marital property election under section 861.02 with respect to the individual property so created. See Wis. Stat. § 766.589(7); see also *infra* § 7.81. Still, the individual property classification under a STIPCA is effective for other purposes: unilateral gifts may be made, and the creation of marital property under the mixing rule or substantial-uncompensated-effort rule of section 766.63 is prevented.

The statute further provides that (1) if, when a STIPCA is executed, property is held as survivorship marital property, the property is classified as the individual property of the owners and is owned as a joint tenancy; and (2) if the property is held in the "and" form or the "or" form described in section 766.60(1) or (2), the property is classified as individual property and is owned as a tenancy in common. Wis. Stat. § 766.589(1)(c)1. If while an agreement is in effect the spouses acquire property as a joint tenancy exclusively between themselves or as survivorship marital property, the property is classified as the owners' individual property and is owned as a joint tenancy. *Id.* If, while an agreement is in effect, the spouses acquire property as tenants in common exclusively between themselves, the spouses' respective ownership interests in the property are classified as the owners' individual property. *Id.* Similarly, if the spouses acquire property held in the "and" form or the "or" form described in section 766.60(1) or (2) while the agreement is in effect, the property is classified as the owners' individual property and is a tenancy in common. Wis. Stat. § 766.589(1)(c)1.

A STIPCA does not affect the incidents of a joint account, as defined in section 705.01(4), under chapter 705. Wis. Stat. § 766.589(1)(c)1. The incident of survivorship is specifically mentioned in the Legislative Council Note to the amendments to this provision in the 1992 Trailer Bill as one of the incidents of a joint account under chapter 705. *See* Wis. Stat. Ann. § 766.589 Legis. Council Notes—1991 Act 301, § 17 (West 2009). Thus, a STIPCA does not destroy the survivorship feature of a chapter 705 joint account. Aside from chapter 705 accounts, to the extent that the incidents of a joint tenancy or a tenancy in common conflict with or differ from the incidents of individual property, the incidents of the tenancy in common or joint tenancy for purposes of a STIPCA, including the incident of survivorship, control. Wis. Stat. § 766.589(1)(c)2.

### **c. Execution [§ 7.76]**

A STIPCA is executed when signed by both spouses and when the signature of each party to the agreement is authenticated or acknowledged. Wis. Stat. § 766.589(2). The requirement of authentication or acknowledgment for a STIPCA differs from that for nonstatutory marital property agreements described in section 766.58. The STIPCA must be in strict conformity with the requirements of the statutory form. Wis. Stat. § 766.589(2); *see* Wis. Stat. § 766.589(10); *see also infra* § 7.178.

### **d. Effective Date and Effective Period [§ 7.77]**

A STIPCA becomes effective when executed or on the determination date (i.e., the date of the spouses' marriage or the establishment by both of them of a domicile in Wisconsin), whichever is later. Wis. Stat. § 766.589(3)(a). If the spouses have not completed the financial disclosure form that appears as Schedule A in the statutory agreement form in section 766.589(10) before or contemporaneously with execution of the agreement, the agreement terminates three years after the date that both spouses sign the agreement unless one of the spouses elects to terminate the agreement earlier under section 766.589(4). Wis. Stat. § 766.589(3)(b). If the spouses have completed the financial disclosure form appearing as Schedule A in the statutory agreement form, the agreement terminates when the terms of the agreement no longer apply after dissolution or the death of a spouse, unless terminated earlier by



one of the spouses under the elective termination provisions of section 766.589(4). Wis. Stat. § 766.589(3)(c). During their marriage, the spouses may enter into only one STIPCA for which disclosure of assets and liabilities is not provided. Wis. Stat. § 766.589(3m).

### **e. Termination by One Spouse [§ 7.78]**

A STIPCA terminates 30 days after a notice of termination is given by one spouse to the other. Wis. Stat. § 766.589(4)(a). An example of the form of a notice of termination is set forth in section 766.589(10). Notice of termination is deemed given to the other spouse on the date that the signed termination is (1) personally delivered to the other spouse, or (2) sent by certified mail to the other spouse's last-known address. Wis. Stat. § 766.589(4)(b).

After notice of termination is given and until the agreement terminates 30 days later, each spouse has the obligation to “act in good faith with respect to the other spouse in matters involving the property of the spouse who is required to act in good faith which is classified as individual property by the agreement.” Wis. Stat. § 766.589(4)(c). However, management and control by a spouse of that property in a manner that limits, diminishes, or fails to produce income from that property does not violate this good faith duty. *Id.*

The statute specifically provides that the unilateral termination right available to each spouse does not affect his or her ability to amend, revoke, or supplement a STIPCA by a separate marital property agreement under section 766.58(4). Wis. Stat. § 766.589(4)(d).

With respect to its effect on third parties, a termination pursuant to section 766.589(4) is treated as a marital property agreement. Wis. Stat. § 766.589(4)(e). Thus, the effect of a termination on creditors' rights would seem to be limited to those creditors who have actual knowledge of the termination or are furnished with a copy of the termination when the obligation to the creditor is incurred. *See* Wis. Stat. §§ 766.55(4m), .56(2)(c).

Termination of a STIPCA does not by itself affect the classification of property acquired before the termination, regardless of whether the termination occurs automatically (as a result of failure to complete the financial disclosure form, the dissolution of the marriage, or the death of

a spouse) or voluntarily (through the unilateral action of one spouse). Wis. Stat. § 766.589(9). Property acquired after the termination is classified as otherwise provided under chapter 766. *Id.*

#### **f. Enforceability [§ 7.79]**

If the spouses do not complete the financial disclosure schedule in the statutory agreement form, *see* Wis. Stat. § 766.589(10), the STIPCA terminates three years after the date that both spouses sign the agreement (unless terminated earlier by either spouse), and despite automatic termination, the STIPCA is enforceable without the disclosure of a spouse's property or financial obligations. Wis. Stat. § 766.589(5)(a). However, if the spouses complete the financial disclosure schedule, ordinarily the STIPCA will be enforceable until the terms of the agreement no longer apply after dissolution or the death of a spouse, unless the agreement is terminated earlier by either spouse or is revoked by a subsequent marital property agreement.

Section 766.589(5)(b) contains an additional limiting factor on the enforceability of agreements for which financial disclosure has been completed. If the spouse against whom enforcement is sought proves that the information on the disclosure form did not provide him or her fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations, the maximum duration of the agreement is three years after the date that both spouses signed the agreement. Wis. Stat. § 766.589(5)(b). This provision applies notwithstanding the fact that the spouse against whom enforcement is sought had notice (i.e., actual knowledge or reason to know) of the other spouse's property or financial obligations. *Id.* The enforceability requirements in section 766.58(6)(c)—namely, that a spouse must receive a fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations, or must have notice of the other spouse's property or financial obligations—are specifically rendered inapplicable to STIPCAs when the financial disclosure schedule has been completed. Wis. Stat. § 766.589(5)(c). Because section 766.58(6)(c) does not apply to a STIPCA containing the requisite financial disclosures, the agreement is enforceable against a spouse unless the latter can prove either unconscionability when the agreement was made or involuntary execution. *See supra* §§ 7.41–.47.

Except to the extent that the statute provides different rules, a STIPCA is subject to the provisions of section 766.58, relating to marital property agreements generally. Wis. Stat. § 766.589(1)(b). Because of the general applicability of the section 766.58 provisions, a STIPCA will not be binding on creditors who do not have actual knowledge of the agreement's provisions. *See* Wis. Stat. § 766.55(4m); *see also supra* § 7.10.

### **g. Effect on Duty of Support During Marriage and at Dissolution of Marriage [§ 7.80]**

The statute makes clear that a STIPCA affects neither the duty of support that spouses otherwise owe each other during marriage nor the determination of property division or maintenance in the event of the marriage's dissolution. Wis. Stat. § 766.589(6). Because it falls within the definition of a marital property agreement in section 766.01(12), a STIPCA also may not affect a spouse's duty to support his or her children. *See* Wis. Stat. § 766.58(2) (discussed in section 7.13, *supra*).

### **h. Effect at Death of Spouse [§ 7.81]**

An important feature of a STIPCA is that it does not affect a spouse's right to exercise the deferred marital property election available under section 861.02. *See* Wis. Stat. § 766.589(7). *See also* the discussion of this election in chapter 12, *infra*. Both predetermination date property meeting the definition of deferred marital property under section 851.055 and property acquired during marriage and after the determination date that would have been marital property but for the agreement are subject to the election. Wis. Stat. § 766.589(7).

The deferred marital property election appears to apply regardless of whether the STIPCA is in effect at the time of, or has terminated before, the death of a spouse who is a party. The important point is that after the termination of a STIPCA by operation of law or by the voluntary action of one of the spouses, all or some of the marital property classified by the agreement as individual property may continue to be subject to a deferred marital property election unless and until reclassified by a subsequent marital property agreement, gift, conveyance, or similar instrument. *See* Wis. Stat. § 766.31(10). In this significant regard,

individual property created by a STIPCA differs from other individual property under the Act.

Regarding creditors, the individual property classification created by a STIPCA is unlikely to affect the property available for satisfaction of obligations at a spouse's death under section 859.18 unless the creditor had actual knowledge of the provisions of the agreement in advance. *See supra* § 7.12.

### **i. Planning Considerations [§ 7.82]**

Without disclosure, a STIPCA will enable spouses moving into Wisconsin for reasons of employment to avoid the marital property laws for up to three years. It will work particularly well when the assignment in Wisconsin will be relatively short or when the newly arriving spouses wish to have time during which to arrange their affairs.

With completion of the disclosure schedule, a STIPCA should suffice as a simple device to classify the spouses' property for estate planning and probate purposes.

It should be possible for one attorney to represent both spouses with regard to a STIPCA regardless of any inequality in their relative economic bargaining power. Dual representation does not present a problem because the agreement (1) is unilaterally terminable by the action of either spouse and (2) preserves statutory elections at death that largely permit the surviving spouse to restore the state of affairs that would have prevailed had there been no agreement.

However, if the spouses desire permanent decisions on property dispositions and a waiver of postdeath elections, a nonstatutory marital property agreement under section 766.58 should be used. Spouses entering into a STIPCA should be warned that the agreement does not prevent the deferred marital property election under section 861.02 from applying if either of them dies before a more comprehensive marital property agreement is entered into or before they establish domicile in another state. Exercise of the deferred marital property elective right by the surviving spouse could disrupt the spouses' existing estate plans.

A STIPCA must be identical to the limited language of the statutory form, virtually ruling out any opportunity to classify certain assets as

marital property and others as individual property or to include special provisions relating to debt satisfaction. As a general rule, if the spouses are willing to make a fair and reasonable disclosure of their property and financial obligations to each other, it is desirable to draft a nonstatutory marital property agreement under section 766.58, because the latter is far more flexible and can be crafted to fit the parties' exact circumstances.

Finally, spouses should be aware that although the statute is silent on the subject, a STIPCA may have the effect of amending or nullifying existing marriage agreements. For example, the spouses may have agreed in an earlier marriage agreement to waive all elective rights against each other's property at the death of either spouse. Execution of a STIPCA may have the effect of reviving those rights. *See* Wis. Stat. § 766.589(7). When existing marriage agreements are involved, a custom-drafted nonstatutory marital property agreement under section 766.58 normally will be advisable.

### **3. Statutory Terminable Marital Property Classification Agreements [§ 7.83]**

#### **a. Introduction [§ 7.84]**

Section 766.588 provides for statutory terminable marital property classification agreements (STMPCAs). A STMPCA's operative effect depends on whether the parties complete a financial disclosure form prescribed in the statutory agreement form, *see* Wis. Stat. § 766.588(9). If the financial disclosure is completed, a STMPCA applies until ended by the dissolution of the marriage, the death of a spouse, unilateral termination by one spouse, or bilateral termination by both. Wis. Stat. § 766.588(3)(c). If the disclosure is not completed, a STMPCA terminates automatically three years after the date of execution, unless ended earlier by unilateral or bilateral action of the spouses. Wis. Stat. § 766.588(3)(b). The STMPCA form is reproduced at section 7.175, *infra*. Without disclosure, a STMPCA has the effect of classifying all of the spouses' presently owned property, and property acquired, reclassified, or created before the agreement's termination, as marital property. If a STMPCA expires by its terms three years after execution, the provisions of the Act apply to the spouses' property. With disclosure, a STMPCA may prove to be a relatively simple device for classifying all of the spouses' property as marital property for estate

planning and probate purposes. Regardless of whether disclosure occurs, a STMPCA may be terminated by the unilateral action of either spouse.

A STMPCA must be identical to the language included in the statutory form. *See* Wis. Stat. § 766.588(2), (9). No variation is permitted. However, the statute explicitly states that section 766.588 is not the exclusive means by which the spouses may reclassify their property as marital property. Wis. Stat. § 766.588(7). Nonstatutory marital property agreements under section 766.58, declarations of gift, conveyances, consents, and unilateral statements are all alternative methods of reclassifying property. *See* Wis. Stat. § 766.31(10); *see also supra* ch. 2.

### **b. Property Law Consequences [§ 7.85]**

Under section 766.588(1)(a), execution of a STMPCA classifies the spouses' presently owned property and property acquired, reclassified, or created in the future, as marital property. The statute contains some special rules for certain assets. For example, notwithstanding the execution of a STMPCA, a nonemployee spouse's marital property interest in a deferred-employment-benefit plan (or the marital property interest in assets in an IRA that are traceable to the rollover of a deferred-employment-benefit plan) terminates at the nonemployee's spouse's death if he or she predeceases the employee spouse. Wis. Stat. § 766.588(1)(b)1. This provision effectively preserves the special terminable interest marital property rule for the nonemployee spouse's interest in a deferred-employment-benefit plan found in sections 766.31(3) and .62(5). (See the discussion of the terminable interest rule in chapter 2, *supra*.) In addition, the marital property interest of a deceased spouse in a life insurance policy designating the surviving spouse as the owner and insured is limited as provided in the frozen interest rule of section 766.61(7). *See* Wis. Stat. § 766.588(1)(b)2.

The statute further provides that if property is held as survivorship marital property under section 766.60(5)(a) or 766.605 when a STMPCA becomes effective, or if property is held or acquired as survivorship marital property under the foregoing sections while the agreement is in effect, the property remains survivorship marital property as long as it is so held. Wis. Stat. § 766.588(1)(c)1. A joint tenancy that is held exclusively between the spouses when a STMPCA becomes effective or while the agreement is in effect is survivorship marital property. Wis.

Stat. § 766.588(1)(c)2. A tenancy in common that is held exclusively between the spouses when a STMPCA becomes effective or while the agreement is in effect is marital property. Wis. Stat. § 766.588(1)(c)3. With respect to tenancies in common or joint tenancies involving either or both of the spouses and a third party at the time a STMPCA becomes effective or while the agreement is in effect, to the extent that the incidents of a tenancy in common or joint tenancy conflict with or differ from the incidents of marital property, the incidents of the tenancy in common or joint tenancy, including the incident of survivorship, control. Wis. Stat. § 766.588(1)(c)4.

Subsection 766.588(1)(d) clarifies that a STMPCA does not affect the treatment of joint accounts and marital accounts under chapter 705. This provision specifically makes clear that a STMPCA (1) does not defeat the survivorship feature of a joint account under section 705.04(1), and (2) does not affect the ownership of sums remaining on deposit in a marital account, as defined in section 705.01(4m), at the death of a party to the account, regardless of when the agreement became effective or the marital account was established. This provision was added to address the concern that, in the absence of the clarifying language with respect to marital accounts under chapter 705, on the death of a spouse a marital account could possibly be allocated 75% to the surviving spouse and 25% to the decedent spouse's estate, rather than divided equally. This could occur if the STMPCA were deemed to affect the chapter 705 treatment of marital accounts. *See* Wis. Stat. Ann. § 766.588 Legis. Council Notes—1991 Act 301, § 16 (West 2009).

### **c. Execution [§ 7.86]**

A STMPCA is executed when signed by both spouses, and when the signature of each party to the agreement is authenticated or acknowledged. Wis. Stat. § 766.588(2). The requirement of authentication or acknowledgment for a STMPCA differs from that for nonstatutory marital property agreements described in section 766.58. The STMPCA must be in strict conformity with the requirements of the statutory form. Wis. Stat. § 766.588(2); *see* Wis. Stat. § 766.588(9); *see also infra* § 7.175.

**d. Effective Date and Effective Period [§ 7.87]**

A STMPCA becomes effective when executed or on the determination date (i.e., the date of the spouses' marriage or the establishment by both of them of a domicile in Wisconsin), whichever is later. Wis. Stat. § 766.588(3)(a). If the spouses have not completed the financial disclosure form that appears as Schedule A in the statutory agreement form in section 766.588(9) before or contemporaneously with execution of the agreement, the agreement terminates three years after the date that both spouses sign the agreement unless one of the spouses elects to terminate the agreement earlier under section 766.588(4). Wis. Stat. § 766.589(3)(b). If the spouses have completed the financial disclosure form appearing as Schedule A in the statutory agreement form, the agreement terminates when the terms of the agreement no longer apply after dissolution or the death of a spouse, unless terminated earlier by one of the spouses under the elective termination provisions of section 766.588(4). Wis. Stat. § 766.588(3)(c). During their marriage, the spouses may enter into only one STMPCA for which disclosure of assets and liabilities is not provided. Wis. Stat. § 766.588(3m).

**e. Termination by One Spouse [§ 7.88]**

A STMPCA terminates 30 days after a notice of termination is given by one spouse to the other. Wis. Stat. § 766.588(4)(a). An example of a notice-of-termination form is set forth in section 766.588(9). Notice of termination is deemed given to the other spouse on the date that the signed termination is (1) personally delivered to the other spouse or (2) sent by certified mail to the other spouse's last-known address. Wis. Stat. § 766.588(4)(b).

The statute specifically provides that the unilateral termination right available to each spouse does not affect his or her ability to amend, revoke, or supplement a STMPCA by a separate marital property agreement under section 766.58(4). Wis. Stat. § 766.588(4)(c).

With respect to its effect on third parties, a termination pursuant to section 766.588(4) is treated as a marital property agreement. Wis. Stat. § 766.588(4)(d). Thus, the effect of a termination on creditors' rights would seem to be limited to those creditors who have actual knowledge of the termination or are furnished with a copy of the termination when



the obligation to the creditor is incurred. *See* Wis. Stat. §§ 766.55(4m), .56(2)(c).

Termination of a STMPCA does not by itself affect the classification of property acquired before the termination, regardless of whether the termination occurs automatically (as a result of failure to complete the financial disclosure form, the dissolution of the marriage, or the death of a spouse) or voluntarily (through the unilateral action of one spouse). Wis. Stat. § 766.588(8). Property acquired after the termination is classified as otherwise provided under chapter 766. *Id.*

#### **f. Enforceability [§ 7.89]**

If the spouses do not complete the financial disclosure schedule in the statutory agreement form, *see* Wis. Stat. § 766.588(9), the STMPCA terminates three years after the date that both spouses sign the agreement (unless terminated earlier by either spouse), and the agreement is enforceable without disclosure of a spouse's property or financial obligations. Wis. Stat. § 766.588(5)(a). However, if the spouses complete the financial disclosure schedule, ordinarily the STMPCA will be enforceable until the terms of the agreement no longer apply after dissolution or the death of a spouse, unless the agreement is terminated earlier by either spouse or is revoked by a subsequent marital property agreement.

Section 766.588(5)(b) contains an additional limiting factor on the enforceability of agreements when financial disclosure has been completed. If the spouse against whom enforcement is sought proves that the information on the disclosure form did not provide him or her fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations, the maximum duration of the agreement is three years after the date that both spouses signed the agreement. Wis. Stat. § 766.588(5)(b). This provision applies notwithstanding the fact that the spouse against whom enforcement is sought had notice (i.e., actual knowledge or reason to know) of the other spouse's property or financial obligations. *Id.* Because of this special statutory provision, the enforceability requirements in section 766.58(6)(c)—namely, that a spouse must receive a fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations, or must have notice of the other spouse's property or financial obligations—are specifically rendered inapplicable to

STMPCAs when the financial disclosure schedule has been completed. Wis. Stat. § 766.588(5)(c). Because section 766.58(6)(c) does not apply to a STMPCA containing the requisite financial disclosures, the agreement is enforceable against a spouse unless the latter can prove either unconscionability when the agreement was made or involuntary execution. *See supra* §§ 7.42, .47.

Except to the extent that the statute provides different rules, a STMPCA is subject to the provisions of section 766.58, relating to marital property agreements generally. Wis. Stat. § 766.588(1)(a). Because of the general applicability of the section 766.58 provisions, a STMPCA will not be binding on creditors who do not have actual knowledge of the provisions of the agreement. *See* Wis. Stat. § 766.55(4m); *see also supra* § 7.10. However, because the universe of assets available to creditors would generally be enlarged, perhaps considerably, by execution of a STMPCA, it is unlikely that creditors would make use of this provision to have such an agreement declared nonbinding.

#### **g. Effect on Duty of Support During Marriage and at Dissolution of Marriage [§ 7.90]**

The statute makes clear that a STMPCA affects neither the duty of support that spouses otherwise owe each other during marriage nor the determination of property division or maintenance in the event of the marriage's dissolution. Wis. Stat. § 766.588(6). Because it falls within the definition of a marital property agreement in section 766.01(12), a STMPCA also may not affect a spouse's duty to support his or her children. *See* Wis. Stat. § 766.58(2) (discussed in section 7.13, *supra*).

#### **h. Effect at Death of Spouse [§ 7.91]**

In contrast to the STIPCA under section 766.589, *see supra* § 7.73, there are no statutory provisions dealing with the effect of a STMPCA at death. That is because the effect of the agreement is to classify as marital property all of the spouses' property owned at the time of the agreement and subsequently acquired. Termination of the agreement does not alter these classifications or restore the status quo ante. With the exception of (1) the interest of a nonemployee spouse in a deferred-employment-benefit plan and (2) the interest of the estate of a nonowner,

noninsured spouse in a life insurance policy, *see* Wis. Stat. § 766.588(1)(b), all of the spouses' assets will be owned as marital property at the death of the first to die, and the usual rules applicable to marital property will apply. The administration of an estate containing marital property is discussed in chapter 12, *infra*. Because all of the spouses' property is classified as marital property, the election of deferred marital property under section 861.02 is unnecessary.

### **i. Planning Considerations [§ 7.92]**

Without disclosure, a STMPCA has the effect of reclassifying as marital property all of the spouses' predetermination date property and individual property owned when the agreement is executed, and all such property acquired before the termination of the agreement. Termination, whether through lapse of time or the voluntary action of one of the spouses, does not alter these reclassifications. Thus, use of this statutory form agreement poses definite risks when one or both spouses wish to preserve certain of their assets as individual or predetermination date property.

With completion of the disclosure schedule, a STMPCA should suffice as a simple device to classify all of the spouses' property as marital for estate planning and probate purposes. Again, the major drawback appears to be the inability to carve out specific assets from the agreement's all-encompassing marital property classification.

A STMPCA must be identical to the limited language of the statutory form, virtually ruling out any opportunity to classify certain assets as individual property or to insert special management and control provisions for specific marital property assets. As a general rule, if the spouses are willing to make a fair and reasonable disclosure of their property and financial obligations to each other, it is desirable to draft a nonstatutory marital property agreement under section 766.58, because the latter is far more flexible and can be crafted to fit the parties' exact circumstances.

Finally, spouses should be aware that, although the statute is silent on the subject, a STMPCA may have the effect of amending or nullifying existing marriage agreements. For example, the spouses may have agreed in an earlier marriage agreement that the property owned by each of them would remain their separate and solely owned property.

Execution of a STMPCA will effectively nullify those arrangements. When existing marriage agreements are involved, use of a custom-drafted nonstatutory marital property agreement under section 766.58 normally is advisable.

#### **4. Statutory Individual Property Classification Agreements [§ 7.93]**

##### **a. In General [§ 7.94]**

The statutory individual property classification agreement (SIPCA) was adopted as section 766.587 by the 1985 Trailer Bill. This statutory marital property agreement was of limited duration and could be entered into without disclosure by either spouse. The SIPCA was designed to prevent the accrual of marital property for up to one year immediately after the Act's effective date to give spouses the opportunity to explore more permanent arrangements for their property. The form of the SIPCA was prescribed by statute. *See* Wis. Stat. § 766.587(7).

##### **b. Property Law Consequences [§ 7.95]**

The SIPCA classified all of the spouses' property, including property owned when the agreement was executed and property acquired after execution but before the agreement terminated, as the owner's individual property. Wis. Stat. § 766.587(1)(a). Ownership of the spouses' property was determined as if it were December 31, 1985. *Id.* Presumably, this provision was intended to define ownership on the basis of the pre-Act common law and statutory rules of title and possession, including the statutory rules regarding the characteristics and creation of joint tenancies and tenancies in common, sections 700.17 and 700.19, because the statutory classification for individual property did not exist on December 31, 1985. The statute further provides that if, while the agreement was in effect, the spouses acquired property as a joint tenancy exclusively between themselves or as survivorship marital property, the property was classified as the owners' individual property and was owned in joint tenancy. Wis. Stat. § 766.587(1)(b). Similarly, if the spouses acquired property and held it in the "and" form or the "or" form described in section 766.60(1) or (2) while the agreement was in effect,

the property was classified as the owners' individual property and was a tenancy in common. *Id.*

The SIPCA classified as individual property both predetermination date property and marital property acquired after the determination date. The importance of this feature was significantly diminished, however, because the reclassification did not prevent the election of deferred marital property under section 861.02 with respect to the individual property so created. Wis. Stat. § 766.587(6). The individual property classification under a SIPCA nonetheless was effective for other purposes: unilateral gifts could be made, and the creation of marital property under the mixing rule or substantial uncompensated effort rule of section 766.63 was prevented. The termination of such agreements by operation of law on January 1, 1987, did not affect the classification of assets acquired before the termination. Wis. Stat. § 766.587(3)(b). Subject to tracing, such assets remained a special kind of individual property subject to the deferred marital property election. Assets acquired after termination that are not traceable to this special individual property are classified as otherwise provided under chapter 766.

The statute contains a specific acknowledgment that it was not the exclusive means by which spouses might classify their property as the owner's individual property before January 1, 1987. *See* Wis. Stat. § 766.587(8). This provision indirectly recognizes that individual property could also result from nonstatutory marital property agreements under section 766.58, gifts, unilateral statements, or consents, as provided in section 766.31(10). Accordingly, section 766.587(8) should not be read as having limited the ability of spouses entering into a SIPCA to reclassify their property to any other form of ownership before or after January 1, 1987.

In a bankruptcy case, a SIPCA was held to provide a sufficient classification basis to trace the nondebtor spouse's individual property, thus precluding the bankruptcy trustee from reaching that property for inclusion in the bankruptcy estate of the debtor spouse. *Ludwig v. Geise (In re Geise)*, 132 B.R. 908 (Bankr. E.D. Wis. 1991).

### **c. Execution and Effective Period [§ 7.96]**

A SIPCA was executed when signed by both spouses. Wis. Stat. § 766.587(2). Persons intending to marry each other could execute a

SIPCA as if married, but the agreement became effective only upon their marriage. Wis. Stat. § 766.587(1)(a). A SIPCA could be executed before, on, or after January 1, 1986, and terminated absolutely on January 1, 1987. Wis. Stat. § 766.587(3).

#### **d. Enforceability [§ 7.97]**

No financial disclosures were required in conjunction with the execution of a SIPCA. The agreement was enforceable without the disclosure of one spouse's property or financial obligations to the other. Wis. Stat. § 766.587(4).

#### **e. Planning Considerations [§ 7.98]**

All SIPCAs terminated absolutely on January 1, 1987. The termination of the agreement by operation of law did not affect the classification of assets acquired before the termination. Because all or part of the individual property created by a SIPCA remains subject to the deferred marital property election under section 861.02 unless and until the property is reclassified, it is desirable for spouses who entered into such agreements to reclassify the individual property so created as "permanent" individual property or as property of some other classification by a subsequent marital property agreement.

### **G. Will Substitute Agreements [§ 7.99]**

#### **1. In General [§ 7.100]**

The provision authorizing will substitute agreements, section 766.58(3)(f), derives from a similar statutory provision in the state of Washington. *See* Wash. Rev. Code § 26.16.120 (West, WESTLAW current with amendments received through January 15, 2010). The Wisconsin enabling provision permits a marital property agreement to transfer existing property and future acquisitions (whether marital property, individual property, predetermination date property, or other) at death without probate by a nontestamentary disposition to a designated person, trust, or other entity. Will substitute provisions may stand alone in a separate agreement or may be included in a marital property agreement containing other provisions.

The basic Wisconsin provision is taken from UMPA section 10(c)(6). The UMPA section 10 comment indicates that the provision is “substantially similar” to that in section 26.16.120 of the Revised Code of Washington, which has been in effect in Washington since 1881. The comment states that this provision “is intended to be used on an omnibus basis with respect to all property, or on a more limited basis with respect to a specified asset or group of assets. It constitutes a statutory authorization for a disposition other than one under the Statute of Wills.” UMPA § 10 cmt. The comment also observes that the provision has roots in the original Uniform Probate Code section 6-201 (now section 6-101), which specifically validated the transfer of assets pursuant to a variety of nonprobate arrangements that did not comply with the formalities required of a will. Under the current version of the Uniform Probate Code, such arrangements include provisions in “an insurance policy, contract of employment, bond, mortgage, promissory note, certificated or uncertificated security, account agreement, custodial agreement, deposit agreement, compensation plan, pension plan, individual retirement plan, employee benefit plan, trust, conveyance, deed of gift, marital property agreement, or other written instrument of a similar nature.” Unif. Probate Code § 6-101. It is of interest that Wisconsin has enacted similar provisions in sections 705.10–.15.

Other states have adopted similar provisions. The concepts of the Washington statute and the Uniform Probate Code provision are both part of Idaho statutory law. *See* Idaho Code § 15-6-201 to 15-6-312 (West, WESTLAW current through (2010) Chs. 1-359 and HJR’s 4, 5 and 7 that are effective on or before April 12, 2010). In 1989, Texas adopted statutory provisions permitting spouses to enter into written community property survivorship agreements. These agreements appear to be much more modest in scope than those permitted in Washington or Idaho. Tex. Prob. Code §§ 451-462 (West, WESTLAW current through the end of the 2009 Regular and First Called Sessions of the 81st Legislature). (The Texas legislature repealed the Texas Probate Code and replaced it with the Texas Estates Code, effective January 1, 2014.)

A key characteristic of will substitute agreements noted by the UMPA section 10 comment is that they cannot be changed during the spouses’ lifetime without mutual consent—and that may be impossible to obtain. It may be possible, however, to draft a will substitute marital property agreement to permit later unilateral withdrawal or reclassification of property by one spouse. Such a feature would add flexibility to will substitute agreements. *See infra* § 7.117.

Section 766.58(3)(f) provides that will substitute provisions (i.e., provisions in a marital property agreement making nontestamentary dispositions of property to the surviving spouse or third parties) are revoked at dissolution of the marriage as provided in section 767.375(1)(a). The latter provision states that, unless the judgment specifically provides otherwise, a judgment of annulment, divorce, or legal separation revokes a will substitute provision providing that, on the death of either spouse, any of either or both spouses' property, including after-acquired property, passes without probate to a designated person, trust, or other entity by nontestamentary disposition. Additionally, under section 767.375(1)(b), a judgment that terminates a marriage also revokes marital property agreement provisions that require either or both spouses to make a particular property disposition in a will or other governing instrument as defined in section 854.01(2). (The latter section includes, among other things, deeds, trust instruments, contracts, insurance or annuity policies, retirement plans, beneficiary designations, instruments of nonprobate transfer under chapter 705, and exercises of a power of appointment.) Dissolution of the spouses' marriage effectively terminates marital property agreement provisions calling for one spouse to make certain transfers to or financial arrangements for the other spouse in the event of the first spouse's death, unless the judgment of annulment, divorce, or legal separation specifically keeps such provisions alive.

The 1985 Trailer Bill added significant additional language to section 766.58(3)(f) not found in UMPA section 10(c)(6). This language allows a surviving spouse to amend a marital property agreement unilaterally with regard to certain property if the agreement provides for the nontestamentary disposition of the property without probate at the surviving spouse's death. The amendment can be made at any time after the first spouse's death but only with regard to property to be disposed of at the second spouse's death. Amendment is not permitted (1) if the agreement expressly provides otherwise, and (2) with respect to property held in a trust specifically established under the marital property agreement. The 1985 Trailer Bill Original Nontax Note to section 766.58(3)(f) indicates that the surviving spouse's right to amend a will substitute agreement unilaterally is warranted to avoid unintended hardship arising from changed circumstances when the surviving spouse outlives the deceased spouse for a substantial time. *See* Wis. Stat. Ann. § 766.58 Legis. Council Notes—1985 Act 37, §§ 112–121 (West 2009). Note that section 766.58(3)(f) does not apply to a will substitute agreement that by its terms requires the surviving spouse to *will* his or



her property to a third person, because the disposition at the second death would be testamentary rather than nontestamentary in nature. There does not appear to be a reason for this distinction.

The unilateral amendment feature presents several practical concerns. For example, most spouses who enter into a marital property agreement making explicit provision for third-party beneficiaries after both spouses' deaths want the certainty of having the arrangement irrevocable, at least as to their existing assets at the first death. Indeed, they may expressly prohibit amendment by the survivor. If they do not, however, neither the statute nor the 1985 Legislative Council Notes give any particulars on the extent of the right of unilateral amendment. It is likely, for example, that the unilateral amendment feature contemplates an unlimited right to invade and consume the property subject to the agreement, but it is not clear that the feature includes the right to transfer such property during lifetime or at death to persons other than the third-party beneficiaries originally designated in the will substitute agreement. It is also uncertain whether invasion under the unilateral amendment feature is limited by an ascertainable standard such as the "health, education, support, or maintenance" standard described in I.R.C. § 2041(b)(1)(A), which would avoid treatment of the right to amend as a taxable general power of appointment in the hands of the surviving spouse. Finally, it is unclear whether the statutory reference to "a trust expressly established under the marital property agreement" includes trusts created independently of the agreement that are designated, by express reference in the terms of the agreement, to receive the property at the death of the first spouse to die.

These major unknowns cause concern in the drafting of will substitute agreements that make any disposition in favor of third parties and that are designed to take effect at the second spouse's death. Furthermore, any effort to draft limitations on the right to invade, consume, or appropriate property—all of which are encompassed within the statutory term "amend"—may have gift tax consequences for the survivor after the first spouse's death. *See infra* ch. 9.

If third parties are named as beneficiaries of a will substitute agreement pursuant to section 766.58(3)(f), and if the agreement expressly precludes spousal amendment, it is likely that the agreement will be directly enforceable by the third-party beneficiaries, because the agreement functions much like a deed or conveyance. For a general discussion of somewhat similar third-party beneficiary contracts to make joint, mutual, and reciprocal wills, see *Chayka v. Santini (In re Estate of*

*Chayka*), 47 Wis. 2d 102, 176 N.W.2d 561 (1970), and *Tilg v. Department of Revenue (In re Estate of Jacobs)*, 92 Wis. 2d 266, 284 N.W.2d 638 (1979). One uncertainty in this type of arrangement is whether the surviving spouse's interest will be likened to a legal life estate or to a trust providing an income interest to the surviving spouse for life, with a remainder passing to the third-party beneficiaries.

Unamendable will substitute agreements naming third parties as beneficiaries at the second death may create even greater difficulties in situations in which the surviving spouse subsequently remarries. It seems reasonably clear that the will substitute agreement will apply to gains from and substitutions for the assets acquired during the first marriage. It is much less clear whether it will apply to the surviving spouse's marital property interest in income and assets acquired during the subsequent marriage or prevent the survivor's new spouse from acquiring a marital property interest in the survivor's earnings or income from property—including the property subject to the will substitute agreement. In addition, it is not clear whether the surviving spouse can enter into a marital property agreement (whether opt-in or opt-out) with his or her new spouse if the agreement will diminish the surviving spouse's assets in any respect.

## **2. Implementation Following Death [§ 7.101]**

Under section 766.58(3m), chapter 854 applies to transfers at death under a marital property agreement. This would include nonprobate, nontestamentary dispositions pursuant to a will substitute agreement described in section 766.58(3)(f). Section 705.10 also governs a variety of nonprobate transfers at death, including those under a will substitute marital property agreement. *See* Wis. Stat. § 705.10(1). Section 705.10(3) provides for applicability of chapter 854 to transfers under this statute. Chapter 854 contains various general rules governing transfers at death but does not contain procedural provisions for effectuating or confirming various nonprobate transfers at death. These provisions are found in sections 867.046(1m), (2), (2m), (3), and 865.201.

Section 867.046 provides simple summary procedures for confirmation of a property interest passing by nontestamentary disposition under a will substitute agreement described in section 766.58(3)(f). The procedures are described in sections 12.172–173, *infra*. The summary confirmation may be either judicial or

administrative. The judicial procedure, which may be invoked by the beneficiary of a will substitute agreement, results in the issuance of a certificate under the seal of the court reciting the fact of death of the decedent, the transfer of the decedent's interest in the property pursuant to the will substitute agreement, the petitioner's interest in the property, and any other facts essential to a determination of the rights of persons interested. Wis. Stat. § 867.046(1m). Alternatively, the beneficiary of a will substitute agreement may use an administrative procedure with the register of deeds to obtain evidence of the termination of the decedent's interest in real property, a vendor's interest in a land contract, an interest in a savings or checking account, an interest in a security, a mortgagee's interest in a mortgage, or an interest in property passing by nonprobate transfer under section 705.10(1) (which includes a marital property agreement), and resulting confirmation of the petitioner's interest in the property. Wis. Stat. § 867.046(2); *see also* Wis. Stat. § 705.10(4).

The protection of payors and other third parties involved in nonprobate transfers of various kinds, including transfers pursuant to a will substitute agreement, is dealt with by section 854.23(1) and (2). As defined in section 854.23(1), a governing instrument includes both a judicial certificate under section 867.046(1m) and an administrative confirmation under section 867.046(2). Insofar as it affects transfers accomplished by will substitute agreement, protection against liability in section 854.23(2) is limited to cases in which a distribution is made to a beneficiary designated in a certificate under section 867.046(1m) or a confirmation under section 867.046(2) who in fact is not entitled to the property and the distribution is made before the payor or other third party receives written notice of a claimed lack of entitlement under chapter 854.

The creation of section 705.10(4) and the amendment of sections 867.046(2) and 854.23(1) in 2006 were intended to reverse or modify key elements of the holding of the Wisconsin Supreme Court in *Maciolek v. City of Milwaukee Employees' Retirement System Annuity & Pension Board*, 2006 WI 10, 288 Wis. 2d 62, 709 N.W.2d 360, *aff'g* 2005 WI App 74, 280 Wis. 2d 585, 695 N.W.2d 875. *See* 2005 Wis. Act 216, §§ 35, 164, 245–47. In *Maciolek*, a stakeholder—in this case the annuity and pension board—was able to require a surviving spouse-beneficiary to use a summary confirmation procedure under section 867.046(1m) or (2) as a condition of releasing funds in its possession directly to the beneficiary.

The drafting committee note to section 705.20(4) (now renumbered section 705.10) states that “[n]o confirmation is required for the non-probate transfer to be valid, but confirmation may be obtained via the informal procedures of §§ 867.046(1m) or (2).” Wis. Stat. § 705.20(4) Committee Note—2005 Wis. Act 216, § 35. At the same time, 2005 Wisconsin Act 216, section 246, broadened the administrative confirmation provisions in section 867.046(2) to include any interest in property passing by nonprobate transfer under section 705.20(1) (renumbered as 705.10(1)), and also broadened the list of persons who might avail themselves of administrative confirmation to include any person having an interest in such property, including a beneficiary under a marital property agreement. This avoids the problem illustrated in *Maciolek*, in which the beneficiary under the marital property agreement was forced into the judicial confirmation proceeding under section 867.046(1m) because the property interest involved was not one of those specifically listed in the former version of section 867.046(2).

In conclusion, it appears that transfers pursuant to a will substitute marital property agreement are self-actuating and valid without any judicial or administrative confirmation. To the extent that a beneficiary under a will substitute marital property agreement wishes to have a confirmation under these statutory provisions, the beneficiary may do so. The protection for third party payors or stakeholders who transfer property pursuant to a will substitute provision in a marital property agreement to a person who in fact is not entitled to the property under provisions of chapter 854, and before the payor or stakeholder receives written notice of the claimed lack of entitlement, is to rely on the nonliability provisions of section 854.23(2).

### **3. Planning Considerations [§ 7.102]**

#### **a. Advantages [§ 7.103]**

A will substitute agreement may prove useful in effectuating a simple “all to the survivor” estate plan for spouses, particularly an older couple, whose estates are small and involve no complex assets or planning considerations. It also is useful when spouses have created a joint revocable trust and transferred substantially all their assets to the trust before the death of the first spouse. Under these circumstances, a will substitute agreement transferring any remaining assets that might otherwise require probate to the trust appears to be a simple and effective

way to avoid probate. Because the will substitute agreement avoids the necessity for probate proceedings, whether formal or informal administration, some savings in time and administrative costs may be achieved. Only a summary proceeding under section 867.046 is required to confirm the transfer of assets pursuant to a will substitute agreement. This proceeding may be either judicial or administrative in nature, at the applicant's option.

To the extent that the will substitute agreement classifies the couple's assets as marital property or survivorship marital property, both spouses' marital property interests will receive a full adjustment in basis at the death of the first spouse to die.

Generally, will substitute agreements containing dispositive provisions for third parties on the surviving spouse's death are more desirable for older couples, because with younger couples there is a much greater likelihood of remarriage if one of the spouses dies. The difficulties of will substitute agreements—particularly those prohibiting or severely restricting withdrawal of assets or amendment—if the surviving spouse remarries are discussed in section 7.104, *infra*.

### **b. Disadvantages [§ 7.104]**

It is likely that the Wisconsin courts will look to Washington and perhaps Idaho precedents in dealing with will substitute agreements. The experience in those states suggests that a number of planning cautions should be observed in drafting such agreements. Many of these cautions apply to the drafting of marital property agreements generally.

1. A will substitute agreement providing that interests in property are created in third parties following the surviving spouse's death raises questions about the nature and attributes of the surviving spouse's estate. *See supra* § 7.100. The surviving spouse's rights to invade or consume the property should be spelled out with specificity to avoid disputes and possible litigation between the spouse and the subsequent beneficiaries. In addition, it is not clear whether the property interest passing to the surviving spouse under a will substitute agreement of this sort qualifies for the federal estate tax marital deduction under the qualified terminable interest property rules, or if the surviving spouse will be deemed to possess broad

powers to invade and consume the property under the general-power-of-appointment rules.

2. Difficulties may be created if the will substitute agreement does not grant the surviving spouse the power to amend the agreement or withdraw property, and the survivor remarries following the first spouse's death. Several categories of property are of particular concern if this occurs: (1) investment earnings (income and gains) on assets comprising the combined estate from the previous marriage; (2) earnings and accumulations of property from the surviving spouse's efforts or labor after the first spouse's death; (3) assets acquired by reason of the surviving spouse's subsequent marriage (i.e., marital property interests in income, earnings, and acquisitions during the subsequent marriage); and (4) assets acquired by the surviving spouse through gift or inheritance after the first spouse's death. It is reasonably clear that the will substitute agreement from the previous marriage should apply to the investment earnings and gains on assets accumulated during the course of that marriage, and perhaps to earnings and accumulations resulting from the survivor's labor or efforts after the first spouse's death. However, the effect of the will substitute agreement on the other categories of assets is unknown. Nor is it clear whether the survivor and his or her new spouse can resolve these problems by executing a marital property agreement. The vested rights of the third party beneficiaries must be taken into account, and the will substitute agreement raises the same problems as does a contract to make a joint, mutual, and reciprocal will. *See supra* § 7.100. If the survivor and his or her new spouse do not have a marital property agreement, an array of new problems will arise upon the survivor's death if the survivor dies before the new spouse. At this juncture, it is likely that the third-party beneficiaries will be pitted against the new spouse. A contest may ensue over (1) the deceased spouse's interest in marital property acquired during the later marriage; (2) whether all or only half the earnings of the now-deceased survivor during the course of the later marriage are subject to the agreement; and (3) the rights of family-purpose creditors to assert claims against the now-deceased survivor with respect to obligations incurred by the new spouse. This catalog of potential problems argues strongly against using will substitute agreements that simultaneously create vested third-party property rights and limit the surviving spouse's ability to withdraw or consume assets or to amend the agreement, particularly when there is a substantial likelihood that the surviving spouse will remarry.

3. A will substitute agreement generally may be revoked only by mutual consent in a subsequently executed marital property agreement, although it may be possible to draft the agreement to permit unilateral withdrawal or amendment. *See, e.g., infra* § 7.117. Absent mutual action by written agreement, a will substitute agreement is irrevocable and indestructible. Typical methods of revoking a will, such as cancellation or physical destruction, are not effective for will substitute agreements.
4. Because a spouse's subsequent incompetence may make it impossible to amend or revoke a will substitute agreement, spouses should enter into the agreement with the full understanding that it may be binding on them forever, regardless of any changes in their circumstances. Section 54.20(2) provides that a guardian appointed for a married person may execute a marital agreement with that person's spouse, subject to the court's approval. The statutory authorization presumably extends to an amendment or revocation of such an agreement. The court's willingness to permit such actions by the guardian may, however, rest upon whether any direct or indirect benefit derives for the incompetent spouse's estate or the natural objects of his or her bounty. *See* Wis. Stat. Ann. § 880.173 Legis. Council Notes—1985 Act 37, § 184 (West 1991). (Section 880.173 has since been repealed and recreated as section 54.20(2)(h).) To avoid these problems, the spouses may wish to consider executing durable powers of attorney to each other that contain specific authority to execute amendments to their will substitute agreement.
5. The typical will substitute agreement is all-encompassing in the sense of transferring both probate and nonprobate property. If the spouses erroneously believe the agreement applies only to probate assets, the agreement's dispositive (and perhaps classification) provisions may conflict with other existing nontestamentary dispositions of those assets by one or both spouses. Ordinarily, the will substitute agreement controls. If, on the other hand, the will substitute agreement is limited by its terms solely to property that otherwise would be subject to administration (i.e., probate assets), the agreement would be open to avoidance by use of nonprobate dispositions.
6. Later execution of an inconsistent will or beneficiary designation by either spouse is ineffective to dispose of any property within the

ambit of a will substitute agreement unless the surviving spouse chooses not to enforce the agreement after the first spouse's death. In addition, the acquiescence itself may have attendant gift tax implications. Execution of a will or a beneficiary designation is a unilateral act, and amendment or revocation of a will substitute agreement requires mutual action by written agreement. Mutual consent to disposition by subsequent will or beneficiary designation would seemingly require either a provision in the original agreement or a subsequent marital property agreement signed by both spouses. Thus, the simple and casually executed will substitute agreement entered into early in marriage and then forgotten about may create serious concerns for later estate planning. It is desirable for estate planners to inquire of both spouses about the existence of prior marital property agreements. *See infra* item 9.

7. If the will substitute agreement purports to dispose of future acquisitions of property, regardless of classification, the parties should give careful consideration to what they might acquire in the future by gift, inheritance, investment success, or earnings. Once the will substitute agreement has been executed, the acquiring spouse normally cannot unilaterally nullify the classification or disposition set forth in the agreement except by gift, if gifts are permitted under the agreement's terms.
8. If the will substitute agreement purports to classify individual property or predetermination date property as marital property (whether when the agreement is executed or at some later date), inherited property or gifts may lose their character and thus not be excludable from a property division under section 767.61 in the event of the dissolution of the marriage. *See, e.g., Bonnell v. Bonnell*, 117 Wis. 2d 241, 344 N.W.2d 123 (1984). Moreover, reclassification may expand the universe of assets available to satisfy creditors.
9. During the course of any estate planning, it may be desirable for the spouses to revoke any outstanding will substitute agreements. Revocation may be accomplished by executing a simple but sweeping marital property agreement to that effect. *See infra* § 7.166. If the spouses are entering into a comprehensive marital property agreement as part of their planning, they may include similar language revoking all prior marital property agreements, including will substitute agreements.



10. Although avoidance of probate through use of a will substitute agreement may save some estate administration costs, these savings must be weighed against the fact that there will be no probate estate for the first spouse to die. A probate estate offers a number of advantages. First, because the probate estate functions as a separate taxpayer, income can be split between the estate and the surviving spouse during the period of administration. Second, having a probate estate may provide some protection against creditors' claims by virtue of the applicability of the statutes in chapter 859 limiting the time for the filing of claims. These provisions appear to provide potentially greater protection for heirs and beneficiaries than the procedures available to creditors under section 859.18 in situations in which a will substitute agreement is used. *See infra* ch. 12. Third, probate provides a mechanism for classifying property, which may be important to determine which assets are marital property and thus qualify for a full basis adjustment. Fourth, it is normally simpler for the personal representative of an estate to transfer assets than for the surviving spouse operating under a will substitute agreement, if only because transfer agents are familiar with the procedures for dealing with transfers by personal representatives.
11. The all-to-the-survivor disposition that often occurs in a will substitute agreement may fail to maximize federal death tax savings by not making use of an applicable exclusion amount (formerly *credit shelter gift*) that escapes taxation at the surviving spouse's death. To obtain the maximum benefit from the federal estate tax unified credits in both spouses' estates, sufficient property has to pass at the first spouse's death in a manner that avoids taxation in the surviving spouse's estate. One example is a family trust that provides the surviving spouse with a discretionary income interest for life, with remainder interests to the children. Such a trust fully uses the unified credit in the estate of the first spouse to die and avoids taxation at the second spouse's death on an amount equal to the value at that time of the assets transferred to the trust.
12. If the spouses separate, a will substitute agreement continues in full force until the court enters a judgment of annulment, divorce, or legal separation, unless a marital property agreement is executed earlier to amend or revoke it.

A sample will substitute agreement is set forth at section 7.163, *infra*.

#### 4. The Washington Experience [§ 7.105]

As discussed in section 7.100, *supra*, section 766.58(3)(f) is based on UMPA section 10, which in turn is derived from section 26.16.120 of the Revised Code of Washington. Accordingly, Washington court decisions concerning statutory community property agreements under the latter statute may be helpful in considering the scope of the Wisconsin provision. The Washington statute permits special statutory agreements by which the spouses may jointly contract “concerning the status or disposition of the whole or any portion of the community property, then owned by them or afterwards to be acquired, to take effect upon the death of either.” Agreements entered into pursuant to this statute are referred to in Washington as *statutory community property agreements*. As special contracts, they are not subject to the laws relating to probate and estate administration and prevail against the deceased spouse’s will. *In re Estate of Brown*, 185 P.2d 125 (Wash. 1947); *McKnight v. McDonald*, 74 P. 1060 (Wash. 1904). Unless rescinded, a recorded statutory community property agreement operates as a conveyance by the deceased spouse to the survivor. *Seeley v. Godfrey (In re Estate of Wittman)*, 365 P.2d 17, 19 (Wash. 1961).

Because they vest immediate ownership of community property in the survivor when the first spouse dies, statutory community property agreements provide a simple nonprobate mechanism for disposing of community property. However, the language of the statute does not require disposition to the surviving spouse; presumably third parties may be beneficiaries as well. See Harry M. Cross, *The Community Property Law in Washington (Revised 1985)*, 61 Wash. L. Rev. 13, 97 (1986).

It has been recognized in Washington that both spouses in a couple may convert separate property to community property and dispose of the property so converted by execution of a statutory community property agreement. *Neeley v. Lockton*, 389 P.2d 909, 912 (Wash. 1964); *Volz v. Zang*, 194 P. 409 (Wash. 1920). By its terms, a statutory community property agreement may also govern the classification of community or separate property acquired after the date of execution, including the conversion of separate property to community property at death. *Brown*, 185 P.2d 125. Such an agreement may cover all or only part of the parties’ property, *see* Wash. Rev. Code. § 26.16.120 (West, WESTLAW current with amendments received through January 15, 2010), provided that what is covered is adequately described. A legal description of real

estate is not required. *Verbeek v. Verbeek*, 467 P.2d 178 (Wash. Ct. App. 1970).

Despite the requirement that a statutory community property agreement can be altered or amended only in the same manner as it was executed, the Washington statute is silent on the issue of revocation or rescission. This has led the Washington Supreme Court to hold that an oral agreement may be effective to rescind a statutory community property agreement when evidence shows that there was a meeting of the minds of the parties to do so. *Seeley*, 365 P.2d 17 (finding no rescission). Conduct manifesting an intention to abandon an agreement also suffices if one party's conduct is inconsistent with the continued existence of the agreement and the other knows and acquiesces in that conduct. *Lyman v. Lyman*, 503 P.2d 1127, 1130–31 (Wash. Ct. App. 1972), *aff'd*, 512 P.2d 1093 (Wash. 1973). The Washington Supreme Court has ruled that legal separation, coupled with an oral agreement to keep separate any acquisitions of property following the separation, has the practical consequence of making the agreement inapplicable to property acquired after the separation. *In re Estate of Janssen*, 351 P.2d 510 (Wash. 1960).

By the same token, the courts in Washington have held that a number of other actions or eventualities do not suffice to revoke a statutory community property agreement. For example, they have held that the subsequent mental incompetency of either of the spouses is not sufficient to avoid the agreement's terms. *Brown's Estate*, 185 P.2d at 129. The filing of a divorce action, by itself, does not serve to abrogate a statutory community property agreement or manifest an intent to abandon the agreement. *Lyman*, 503 P.2d at 1131–32.

Washington courts have held that the mere making of a subsequent inconsistent will or codicil by one of the spouses is insufficient to constitute a revocation or abandonment of a statutory community property agreement. *See Lyman*, 503 P.2d at 1132; *Seeley*, 365 P.2d 17.

In *Neeley v. Lockton*, 389 P.2d 909 (Wash. 1964), the Washington Supreme Court made clear that the provisions of a statutory community property agreement are superior to any conflicting beneficiary designation on life insurance or retirement plan benefits that are subject to the agreement's terms. The court stated that Washington's community property law will control over inconsistent contracts. According to the court, the statutory community property agreement is a vital element of Washington's community property law and furthers the policy of

providing a simple and certain method of disposing of the community property upon the death of either spouse. *Id.* at 912. Of note is the fact that the beneficiary designation in *Neeley* predated the community property agreement. *Neeley* was followed by the court in *Harris v. Harris*, 804 P.2d 1277 (Wash. Ct. App. 1991), which held that a community property agreement controls over a prior beneficiary designation for a retirement annuity. A divorce decree had awarded the retirement annuity to the employee-husband. However, the husband failed to change the beneficiary designation that named his former wife as beneficiary. Subsequently, the husband remarried and entered into a statutory community property agreement with his second wife. The court held that the statutory community property agreement converted the retirement annuity into community property and provided for the immediate transfer of the husband's community property interest at death to the second wife despite the inconsistent beneficiary designation.

In view of the lack of recognition given to subsequent conflicting wills and codicils and the strong language in *Neeley*, it is unlikely that the Washington courts will permit subsequent conflicting beneficiary designation changes with respect to life insurance policies or retirement plan benefits to prevail over the contrary provisions of an earlier statutory community property agreement. In fact, the Washington courts have refused to permit a subsequent conveyance by one spouse to his children that was inconsistent with a previously executed statutory community property agreement. *Bosone v. Bosone*, 768 P.2d 1022 (Wash. Ct. App. 1989).

A caveat is needed here with regard to the import of the Washington cases discussed above with respect to prior or subsequent conflicting beneficiary designations for retirement benefits under ERISA-qualified plans. As a result of the U.S. Supreme Court decision in *Boggs v. Boggs*, 520 U.S. 833 (1997), it appears that provisions of state community property law no longer will control over conflicting attributes and requirements of federal law governing ERISA-qualified retirement plans. (See also section 9.64, *infra*, for a detailed discussion of the impact of *Boggs* on qualified retirement plans.) Thus, to the extent that beneficiary provisions are mandated by ERISA, as amended by the Retirement Equity Act of 1984 (REA), they may not be overridden by a Washington community property agreement. See generally ERISA, 29 U.S.C. §§ 1001–1461; REA, Pub. L. No. 98-397, 98 Stat. 1426.

In a few cases, however, the subsequent inconsistent conduct of one or both of the spouses, viewed in the context of surrounding circumstances, did evince an intention to abandon the statutory community property agreement or to waive its benefits. See *Estate of Wahl v. Sharp (In re Estate of Wahl)*, 644 P.2d 1215 (Wash. Ct. App. 1982), *aff'd*, 664 P.2d 1250 (Wash. 1983) (holding that execution of inconsistent codicils on same date as statutory community property agreement raised question of fact as to spouses' intent). In *Norris v. Norris*, 622 P.2d 816 (Wash. 1980), the spouses first executed reciprocal wills and later executed an inconsistent statutory community property agreement without the benefit of legal advice. Following the wife's death, the husband became the personal representative and rejected the agreement for tax reasons. The court held that because the husband had accepted benefits under the will, he was deemed to have waived the agreement.

The Washington Court of Appeals held that the transfer of real estate from one spouse to the other, with the recital that it was to be the transferee's sole and separate property, constituted a partial revocation of a statutory community property agreement, at least with respect to the real estate conveyed. *In re Estate of Ford*, 639 P.2d 848, 850 (Wash. Ct. App. 1982). The court inferred a mutual intent to modify the agreement from one spouse's execution of the deed and the other spouse's acceptance of that deed. *Id.*

The question posed in *Higgins v. Stafford*, 866 P.2d 31 (Wash. 1994), was whether a community property agreement was rescinded or abandoned when the parties, 10 years after executing the agreement, executed mutual wills and a comprehensive agreement regarding the disposition of their community property upon the deaths of each of them. The court held that as long as a mutual intent to abandon or rescind a prior community property agreement is adequately established, mutual wills may control over a prior community property agreement, whereas unilateral acts by one spouse alone inconsistent with the community property agreement are not enough. The court concluded that the will agreement and mutual wills were squarely in conflict with the earlier community property agreement and that the spouses intended the will agreement and mutual wills to control the disposition of their property. Accordingly, the community property agreement was deemed rescinded.

Dissolution of a marriage does not automatically terminate the spouses' statutory community property agreement under the Washington

statute. Washington has a statutory provision providing for “just and equitable” disposition of community and separate property on dissolution. Wash. Rev. Code Ann. § 26.09.080 (West, WESTLAW current with amendments received through January 15, 2010). Presumably, however, a court decree dissolving the marriage can provide for cancellation of a statutory community property agreement. *See Lyman*, 503 P.2d at 1131–32.

## **5. Comparison of Washington and Wisconsin Statutes [§ 7.106]**

Unlike the Washington statute, section 766.58(3)(f) applies to “any of either or both spouses’ property, including after-acquired property,” and not just to assets classified as marital property. The difference is that the Washington statutory community property agreement requires the specific reclassification of separate property to community property, either when the agreement is entered into or subsequently, to make the agreement operate on the property. *See Volz v. Zang*, 194 P. 409 (Wash. 1920). No such reclassification is required under the Wisconsin statute. Further, the Washington statute does not specify who or what may be the transferee under a disposition by agreement, although one leading analyst of Washington’s community property laws believes that dispositions other than to the surviving spouse are permissible. *See Cross, supra* § 7.105, at 97. Section 766.58(3)(f) specifically states that the dispositive provisions may be “to a designated person, trust or other entity.” Finally, the Washington statute does not contain language granting a surviving spouse the right of unilateral amendment when the agreement purports to dispose of property at the surviving spouse’s death.

In Washington, a will substitute agreement may be abandoned or revoked by oral understanding if the parties’ actions are consistent with the oral understanding. *See supra* § 7.105. The Wisconsin statute, section 766.58(4), specifically requires revocation by another marital property agreement. It is not known whether the Wisconsin courts will apply the doctrines of contractual abandonment or part performance to avoid serious inequity when the parties attempt a nonwritten revocation; the decision in *Brandt v. Brandt*, 145 Wis. 2d 394, 427 N.W.2d 126 (Ct. App. 1988), a divorce case, suggests that they may. In *Brandt*, the court viewed repeated failures to observe a marriage agreement, or to mention it or take it into account in the course of subsequent financial and estate planning, as an abandonment of the agreement. *Id.* at 415–16.

Washington's statute is silent on how dissolution of the marriage affects a will substitute agreement. The Wisconsin statutes provide that a judgment of dissolution revokes both a will substitute provision in a marital property agreement and other marital property agreement provisions requiring one spouse to make certain transfers to or financial arrangements for the other spouse in the event of the first spouse's death, unless the judgment provides otherwise. *See* Wis. Stat. §§ 766.58(3)(f), 767.375(1) (discussed in sections 7.23 and 7.100, *supra*). As noted in section 7.104, *supra*, and section 7.114, *infra*, a will substitute agreement reclassifying existing or future individual property assets received by inheritance or gift as marital property may cause the reclassified assets to be included in the property division under section 767.61 in the event of dissolution.

Just as the Washington statute protects creditors' rights, so do sections 766.55(4m) and 859.18(6) with respect to marital property agreements (including will substitute agreements). Section 766.58 does not, however, preclude creditors' rights from being enhanced. For example, a marital property agreement providing for immediate conversion of after-acquired individual property into marital property would likely make that property available for satisfaction of a judgment rendered against the other spouse for an obligation incurred in the interest of the marriage or the family. *See, e.g., Merriman v. Curl*, 509 P.2d 765 (Wash. Ct. App. 1973).

## **H. Effect of Marital Property Agreements at Dissolution of Marriage [§ 7.107]**

Two 1986 decisions of the Wisconsin Supreme Court, *Button*, 131 Wis. 2d 84, and *Schumacher*, 131 Wis. 2d 332, set the standards for enforceability of marriage agreements under section 767.61(3)(L) (formerly numbered section 767.255(3)(L) and (11)), the statutory provision relating to property divisions at dissolution. Neither of these decisions involved marital property agreements as defined in the Act. Because the requirements for validity and enforceability of marital property agreements under sections 766.58, .585, .588, and .589 differ somewhat from the requirements for validity and enforceability of marriage agreements entered into before the effective date of the Act, *see infra* §§ 7.122–.131, .133–.140, further modification in the law may occur.

The Wisconsin Supreme Court's first consideration of the effect of a post-1985 marital property agreement in a divorce action occurred in *Steinmann v. Steinmann*, 2008 WI 43, 309 Wis. 2d 29, 748 N.W.2d 145. This case did not involve the validity or enforceability of the marital property agreement (both of which were conceded), but rather the implications of classification, tracing, and change of character of assets for the property division. In *Steinmann*, the husband and the wife had entered into what was denominated a limited marital property classification agreement following their marriage in 1994. The agreement classified various assets and income into categories of "marital property," "survivorship marital property," "individual property of [husband]" and "individual property of [wife]" and provided that property acquired with individual property, in exchange for individual property, or with the proceeds of individual property remained individual property. The marital property agreement was silent as to maintenance obligations in the event of dissolution of the marriage, but specified that it would be binding on the question of property division. The agreement provided that it could be modified or waived "by written instrument duly subscribed and acknowledged by the parties." *Id.* ¶¶ 5–6.

During the marriage, a large litigation settlement payable jointly to the husband, the wife, and the wife's solely owned business was deposited into the wife's individual property bank account. The funds were then used to acquire a number of significant assets titled in the joint names of the spouses. In the divorce action, the wife contended that the circuit court should apply tracing principles to funds that had been deposited in the individual property bank account, while the husband contended that transmutation principles should be applied to determine that the funds had been reclassified into jointly held marital property that was divisible in the divorce action.

The Wisconsin Supreme Court declined to attempt to harmonize the marital property classification principles of chapter 766 with the equitable property division principles of chapter 767, stating as follows:

[M]arital property classification, governed by ch. 766, is generally a separate inquiry from equitable property distribution, governed by ch. 767. *See Lloyd v. Lloyd*, 170 Wis. 2d 240, 258 & n.6, 487 N.W.2d 647 (Ct. App. 1992). Unfortunately, the parties' marital property classification and divisibility arguments overlap, blurring the distinction between the two issues and chapters. Blurring the distinction even more is the face of the Agreement itself, which is titled under ch. 766 and primarily addresses property classification, but which also states that it is binding on ch. 767 property



division determinations. The interrelationship between the two statutory chapters in such a context has not been explicitly addressed by the parties. *We therefore do not resolve in this case the exact nature of the relationship between chs. 766 and 767 in cases such as this one in which ch. 767 equitable property distribution determinations include consideration of ch. 766 marital property agreements, and in which marital property classification might be relevant to division. Rather, we focus on the tracing and transmutation arguments as presented by the parties.* (Emphasis added.)

*Id.* ¶ 28.

The court went on to reject the wife’s tracing argument in favor of holding that the acquisition of several valuable real-property assets in joint tenancy effectuated a transmutation of what might otherwise have been individual property funds into divisible marital property for purposes of section 767.61(2). The court noted that “when separate property [i.e., individual property] presumed to be indivisible is transmuted through a joint tenancy, it is effectively transferred to marital property, and tracing does not cause the property to revert back to its original separate property identity.” *Id.* ¶ 35. In reaching its conclusion, the court discussed *Trattles v. Trattles*, 126 Wis. 2d 219, 376 N.W.2d 379 (Ct. App. 1985); *Brandt v. Brandt*, 145 Wis. 2d 394, 427 N.W.2d 126 (Ct. App. 1988); *Fowler v. Fowler*, 158 Wis. 2d 508, 463 N.W.2d 370 (Ct. App. 1990); and *Derr v. Derr*, 2005 WI App 63, 280 Wis. 2d 681, 696 N.W.2d 170. The court also noted that it did not limit its holding in *Bonnell v. Bonnell*, 117 Wis. 2d 241, 246–47, 344 N.W.2d 123 (1984) only to gifted or inherited property, indicating that the “decision spoke in broader terms about joint tenancies being valid transmutations of separate property [i.e., individual property], *whatever* the prior ownership interests of each party.” *Steinmann*, 2008 WI 43, ¶ 37, 309 Wis. 2d 29 (citation omitted). The court also noted that there was no compelling policy reason for rendering transmutation or donative-intent principles inapplicable to property initially classified as individual property under a marital property agreement. *Id.* ¶ 38.

Finally, the court observed that section 766.31 explicitly allows property classified as individual property under a marital property agreement (as well as gifts, inheritances, and other forms of individual property) to be reclassified as marital property by gift, deed, or other conveyance, thus specifically sanctioning the type of reclassification from which the wife claimed her property was exempt. *Id.* ¶ 43 n.16. Accordingly, the transmutation/reclassification/donative intent evidenced

by the spouses' acquisition of various real estate assets in joint tenancy was held to trump the application of tracing principles in effectuating a property division in the divorce. *Id.* ¶¶ 42–52.

It should be noted that the only other appellate case involving enforceability of a post-effective-date marital property agreement at dissolution is an unpublished decision, *Weissgerber v. Weissgerber*, No. 03-0093, 2004 WL 1534191 (Wis. Ct. App. July 8, 2004) (unpublished opinion not citable per section 809.23(3)), in which the court's discussion revolved exclusively around the requirements of section 767.61(3)(L) (formerly 767.255(3L)), *Button*, and *Schumacher*, with no mention made of the enforceability standards set forth in section 766.58(6).

One important issue that may require attention is whether the section 767.61(3)(L) “equitableness” requirement with respect to the enforceability of marriage agreements in the event of dissolution should be harmonized with the section 766.58(6) requirements for enforceability of a marital property agreement. The enforceability standards in section 766.58(6) focus on the time immediately preceding and at the making of the agreement. The section 767.61(3)(L) equitableness test may have a different focus. In *Button*, 131 Wis. 2d 84, the supreme court held that the substantive fairness portion of the equitableness test would be determined at the time of execution of the agreement, and also at the time of dissolution, if circumstances significantly changed after the execution of the agreement in a manner not reasonably foreseen or foreseeable by the parties. Thus, equitableness in the context of an action for dissolution may be determined at the time of the divorce, as well as at the time when the agreement was made. This results in a dual standard for enforceability of marital property agreements—that is, the standard set forth in section 766.58(6) applies during the marriage or at death and the standard arising by judicial interpretation of section 767.61(3)(L) applies at the dissolution of the marriage. The language of section 766.58(6) does not itself confine the enforceability standards for marital property agreements to the ongoing marriage or the death of a spouse, thus giving rise to the need for clarification of its relationship to section 767.61(3)(L). For a more complete discussion of the enforceability standards that apply at divorce to agreements entered into before the Act became effective, see sections 7.133–.140, *infra*.

It is also worthy of note that section 767.56(8), relating to the determination of maintenance in dissolution proceedings, requires only

that the family court “consider” spousal support arrangements contained in a marriage agreement. Thus, the court is free to reject those arrangements if it chooses. *See infra* ch. 11.

## **I. Planning Considerations with Respect to Marital Property Agreements [§ 7.108]**

### **1. In General [§ 7.109]**

The requirements for a valid and enforceable marital property agreement are discussed in sections 7.15–.70, *supra*. To summarize, a valid marital property agreement must be

1. A document signed by both spouses, but only by both spouses and no third parties;
2. Not unconscionable when made;
3. Executed voluntarily;
4. Accompanied either by fair and reasonable disclosure under the circumstances of each spouse’s property and financial obligations, or, alternatively, by actual knowledge or reason to know of the other spouse’s property or financial obligations before execution of the agreement; and
5. Equitable as to both parties if it is to be enforceable as a property settlement agreement in the event of the dissolution of the marriage, *see infra* §§ 7.133–.140 (discussion of equitableness in context of pre-Act marriage agreements).

For additional resources concerning the drafting of marital property agreements, see, for example, Leonard L. Loeb et al., *System Book for Family Law*, ch. 14G (State Bar of Wisconsin CLE Books 6th ed. 2007 & Supp.), and Mark J. Bradley et al., *Eckhardt’s Workbook for Wisconsin Estate Planners* ch. 9 (State Bar of Wisconsin CLE Books 5th ed. 2008). Sections 7.110–.118, *infra*, discuss various considerations relating to planning and drafting marital property agreements. Sample forms of various kinds of marital property agreements are found in sections 7.148–.178, *infra*.

## **2. Marital Property Agreements to Adopt System of Property Ownership Based on Title or to Classify All or Most Assets as Individual Property**

**[§ 7.110]**

### **a. Advantages and Disadvantages [§ 7.111]**

Either before or after the determination date, spouses or persons intending to marry may wish to execute a marital property agreement either to adopt a system of property ownership based on title or to classify all or most assets as individual property. The broad contractual freedom extended by sections 766.17(1) and 766.58(3) clearly countenances this. A number of reasons might exist for such an agreement. The spouses might wish to

1. Limit (to the extent possible) future creditors' ability to reach the assets or income of one spouse to satisfy obligations incurred by the other spouse in the interest of the marriage or the family after the determination date;
2. Provide certainty as to the classification of their property when one of the spouses dies and thus avoid the need for tracing, the presumptions in favor of marital property, and the deferred marital property election statutes;
3. Avoid the need for extensive revision of their current estate plans;
4. Ensure that the disposition of specific assets to certain beneficiaries at death will occur as intended;
5. Maintain wealth existing at the time of remarriage for children of a prior marriage;
6. Ensure that adequate management arrangements for certain assets will continue after the death of a spouse presently having title to those assets;
7. Maximize the use of the titled spouse's estate as a separate taxpayer to the extent that there are benefits to be derived from doing so;

8. Preserve maximum postmortem tax planning opportunities for the estate of the spouse with more property through the availability of elections (such as the qualified terminable interest property (QTIP) election) and disclaimers;
9. Make gifts of assets that otherwise might be subject to recovery under section 766.70 because they would have been marital property or would have had a marital property component; or
10. Take advantage of a combination of these factors.

There are also disadvantages that might result from executing an agreement to maintain a system of property ownership based on title or to classify all or most assets as individual property. These include

1. Losing the opportunity for the full adjustment in basis that is available for both spouses' interests in marital property upon the death of one of them, *see infra* ch. 9;
2. Giving up rights or remedies relating to the management and control of assets or income held or acquired by the other spouse that would have been marital property but for the agreement;
3. Losing access to credit that otherwise might have been available to a spouse through classification of assets (particularly the other spouse's income) as marital property;
4. Giving up any protections of the good-faith duty imposed on the other spouse with respect to matters involving assets that otherwise would have been marital property;
5. Giving up the right to will one-half the value of any assets titled in the other spouse's name that otherwise would have been marital property to persons of the deceased spouse's choice;
6. Giving up various interspousal remedies available concerning property that otherwise would have been marital property, including the right to recover unilateral gifts of such property exceeding \$1,000 (or larger reasonable amount) in a given year as provided in section 766.53; and

7. Possibly losing for the less-propriety spouse any elective right against the other spouse's estate if the other spouse dies first and leaves his or her property to third parties, unless the agreement contains specific financial provisions for the less-propriety spouse.

### **b. Drafting Approaches [§ 7.112]**

There are several different approaches to drafting an agreement to continue a system of property ownership based on title or to otherwise opt out of the Act to some significant degree. *See supra* § 7.14 (certain statutory limitations on opting out). Each approach has advantages and disadvantages. The primary methods are the following:

1. Enter into a section 766.589 STIPCA with disclosure. These agreements and their legal consequences are discussed in detail in sections 7.73–82, *supra*; the form is reproduced at section 7.178, *infra*. The STIPCA reclassifies marital property, whether presently existing or acquired in the future, as the owner's individual property. Ownership is determined on the basis of how the property is held. *See supra* ch. 4 (discussion of principles of holding property). If property classified by a STIPCA is not held by either or both of the spouses, ownership is determined as if the spouse were unmarried when the property was acquired. Additional rules are provided for marital property assets held by both spouses. Although execution of a STIPCA is relatively simple, the agreement is inflexible and not subject to variation to fit the spouses' individual circumstances. Moreover, it is terminable by the unilateral action of one of the spouses and applies the deferred marital property election under section 861.02 not only to all deferred marital property but also to all individual property acquired during the marriage and after the determination date that would have been marital property but for the agreement. Wis. Stat. § 766.589(7); *see supra* § 7.82 (more detailed discussion of planning limitations of STIPCA's).
2. Adopt the common law and statutory property ownership rules in effect on December 31, 1985. This was the classification method used in the now-defunct statutory individual property classification agreement in section 766.587, discussed in sections 7.93–98, *supra*. Property owned by married persons would continue to be owned either solely, as a tenancy in common, or as a joint tenancy with right of survivorship, all determined under the rules of ownership that applied immediately before the Act. Such an agreement has the

advantages of relative simplicity and working with a defined and ascertainable body of law. Its disadvantage is that the body of law is fixed and static and will not be developing in response to changing conditions. In time, the property law system in effect on December 31, 1985, for married persons may be forgotten by nearly everyone. Although an agreement of this sort could be as simple or as complex as the drafter cares to make it, one issue that almost certainly must be dealt with is whether the prior spousal elective rights found in sections 861.03–.13 (1983–84) are to apply. The agreement should specifically state whether these spousal elective rights are included as part of the property ownership rules on December 31, 1985, because the statutes from which they derive have been repealed.

3. Classify the spouses' property as their individual property based on rules of title, acquisition, or possession spelled out in the agreement. The thrust of the agreement is that property titled in one spouse's name, acquired with consideration furnished by one spouse, or possessed exclusively by one spouse, is that spouse's individual property. Property titled or acquired in both spouses' names might be classified as joint tenancy with right of survivorship, as tenancy in common, as survivorship marital property, or as marital property, depending on the spouses' desires. An agreement styled in this manner has the advantage of using as its primary form of ownership a property classification created and defined by the Act, namely, individual property. Thus, its attributes should continue to be reasonably well understood with the passage of time. The drawbacks are that if the attributes of individual property are significantly changed by subsequent legislation or court decision, the expectations of one or both parties might be adversely affected. Similarly, if both spouses move to a non-community property state, property of a classification not recognized under the laws of the new domiciliary jurisdiction might continue to be created under the agreement's terms unless provisions are included in the agreement to address this problem. Finally, an agreement of this sort must necessarily address the issue of what dispositions of individual property will be made at death in favor of the surviving spouse to replace the statutory elective share and support provisions that presumably are negated by the agreement.
4. Classify the spouses' property as their common law solely owned property as if they were unmarried persons, based on rules of title, acquisition, or possession that are spelled out in the agreement. In

short, property titled in one spouse's name, acquired with consideration furnished by one spouse, or possessed exclusively by one spouse, is that spouse's solely owned property. Property owned by unmarried persons will of course continue to be common law solely owned property governed by an evolving mixture of common law and statutory rules. Applying this evolving body of law by agreement to the assets of married persons affords an advantage to this fourth method not enjoyed by the second method discussed above, which uses a static property law system fixed in time and content. One disadvantage of the fourth method is that it relies on a legal fiction (i.e., it treats the parties as unmarried persons when in fact they are or are about to be married), which some contracting spouses may dislike. Second, the method creates and uses a property law classification not described in the Act (although that clearly seems permissible under the broad contractual freedom extended to spouses by section 766.17(1)). *See supra* § 7.6. Third, because a spouse treated as an unmarried person has no rights against the other spouse's estate, the agreement should either contain an adequate financial provision for the surviving spouse or contractually set up a mechanism for spousal elective rights at death.

A sample agreement to adopt a system of property ownership based on classification of most or all assets as individual property (method 3 above) is set forth in section 7.154, *infra*. The inclusion of an agreement employing this particular approach does not imply that the authors prefer that approach over the others.

A spouse who owns (or will own) the most significant assets in the marriage or who generates the most significant income may be tempted to rely on full disclosure and voluntary execution alone to support an opt-out marital property agreement that makes no provision or only a minimal provision for his or her spouse at the termination of the marriage by death. This ignores the first of the section 766.58(6) requirements for enforceability, namely, that the agreement must not be unconscionable when made. The concept of unconscionability is broad and vague, *see supra* § 7.42, and at this juncture there are no Wisconsin precedents defining it in the context of marital property agreements. The mere fact of economic one-sidedness does not alone establish unconscionability. If, however, a great disparity in economic wealth exists between the parties, an agreement that makes no financial provision for a spouse at the termination of the marriage could possibly give the appearance of overreaching. That in turn might subject the agreement to closer-than-



usual scrutiny. If a court determined that there had been overreaching or oppression, it might refuse to enforce the agreement on grounds of unconscionability. *See supra* § 7.42.

### **3. Marital Property Agreements to Classify All or Most Assets as Marital Property [§ 7.113]**

#### **a. Advantages and Disadvantages [§ 7.114]**

Married couples (and couples intending to marry) may elect to enter into marital property agreements classifying all or substantially all of their assets as marital property, in order to bring them fully within the provisions of the Act. This may be predicated on a desire to

1. Bring property-sharing principles into their marriage for philosophical reasons, both as to assets acquired before the determination date and those subsequently acquired;
2. Provide certainty as to the classification of their property when one of the spouses dies;
3. Equalize their estates for tax-planning reasons;
4. Obtain a full basis adjustment for their marital property assets on the death of the first spouse to die, *see infra* § 9.24;
5. Provide greater access to credit for the spouse with fewer assets;
6. Equalize the assets available to each spouse for testamentary disposition; or
7. Take advantage of a combination of these factors.

In preparing an agreement that classifies all assets as marital property, several possibly adverse consequences should be kept in mind:

1. If one or both of the spouses have (or expect to receive) significant property by way of inheritances or gifts, the reclassification of all such property as marital property may cause it to be included in a property division in the event of the dissolution of the marriage. In

other words, when reclassified by agreement under section 766.31(10), the property may lose its character as a gift from a third party or transfer by reason of the death of another for purposes of the exclusion under section 767.61(2). *See, e.g., Bonnell v. Bonnell*, 117 Wis. 2d 241, 344 N.W.2d 123 (1984).

2. Classification of all property as marital property increases the pool of assets available to creditors for family-purpose obligations incurred by either spouse. *See supra* chs. 5, 6.
3. In making unilateral gifts of property that formerly was individual property or predetermination date property but now is classified as marital property, each spouse is limited to the \$1,000 amount (or a larger reasonable amount) in a given year as provided in section 766.53 if the other spouse does not consent.
4. The spouse who formerly had the larger estate partially gives up the right to dispose of assets by will and may lose some access to credit.
5. If one of the spouses has significantly more property than the other, entering into an agreement classifying most or all of the spouses' existing assets as marital property often will result in an immediate gift from the spouse with more property to the spouse with less property. *See Rev. Rul. 77-359, 1977-2 C.B. 24*. An outright gift of this sort from one spouse to the other ordinarily will cause no adverse federal gift tax consequences because of the availability of the gift tax marital deduction. *See I.R.C. § 2523*. However, if the less-propertied donee spouse is not a United States citizen, the marital deduction is disallowed, and gift amounts in excess of a specified amount will be subject to tax.

### **b. Drafting Approaches [§ 7.115]**

There are several different approaches to preparing an agreement to classify all or most of the spouses' assets as marital property. Each has advantages and disadvantages. The primary methods are the following:

1. Enter into a section 766.588 STMPCA with disclosure. These agreements and their legal consequences are discussed in detail in sections 7.83–.92, *supra*. The STMPCA classifies all presently owned property of the spouses, and all property acquired,

reclassified, or created in the future, as marital property without regard to whether such property otherwise would have been marital property under the provisions of the Act. Although execution of a STMPCA is a relatively simple proposition, the agreement has the twin deficiencies of inflexibility (it is not subject to any variance) and uncertainty (it is unilaterally terminable by either spouse). For a more detailed discussion of the planning limitations of STMPCA's, see section 7.92, *supra*.

2. Create a custom-drafted marital property agreement classifying most or all of the spouses' property as marital property. Custom-drafted agreements have obvious attractions. However, in preparing such an agreement, the drafter must be cognizant of the need to define the desired attributes of "marital property" as that classification is applied to various assets. This results from the fact that Wisconsin does not have a "pure" system of community (i.e., marital) property. The basic rule set forth in section 766.31(3) is that each spouse owns a present undivided one-half interest in each item of marital property. This one-half interest may be disposed of at death. Nonetheless, the exceptions and variations to the general rule commence almost immediately after it is stated. For example, the second clause of section 766.31(3) creates a terminable interest rule for the nonemployee spouse's marital property interest in a deferred employment benefit plan or rollover IRA. *See also* Wis. Stat. § 766.62(5). If the nonemployee spouse dies first, his or her marital property interest simply terminates and cannot be disposed of by will or otherwise. Sections 861.01(3m) and 766.31(7m) contain a comparable rule for recoveries for loss of future income arising from a personal injury when the noninjured spouse dies first. Further, a deceased spouse's marital property rights in a life insurance policy owned by and insuring the surviving spouse may be limited by section 766.61(7). *See supra* § 2.95. With respect to homestead real estate, section 766.605 provides that a homestead acquired after the determination date in both spouses' names is survivorship marital property that passes automatically to the survivor at death if no intent to the contrary is expressed on the instrument of transfer or in a marital property agreement. Finally, the marital property portion of life insurance policies and proceeds and deferred employment benefits is determined in accordance with special time-based apportionment rules contained in sections 766.61 and 766.62, respectively. These special rules and exceptions affect a spouse's right either to dispose of his or her undivided one-half interest at

death or to change the ownership fraction to something other than equal one-half interests. All of these rules are clearly part and parcel of marital property under the Act, but they may not all be desired or desirable in an opt-in marital property agreement.

An agreement defining marital property as a present undivided one-half interest in each asset owned by the spouses would create a relatively simple and universal marital property system. However, it would not be identical to marital property as found in chapter 766. In entering into an agreement to classify all or most of their property as marital property, the spouses may pick and choose among the Act's special rules: they may wish to follow the pure undivided one-half interest rule instead of the special apportionment rules otherwise applicable to each spouse's life insurance policies and deferred employment benefits; they may wish to negate the terminable interest marital property rule that applies under the Act to the nonemployee spouse's interest in a deferred-employment-benefit plan; they may wish to negate the survivorship feature that otherwise applies to their marital property personal residence; or they may wish to allow an insurance policy on the surviving spouse's life to be treated as "regular" marital property, rather than as subject to the frozen interest rule of section 766.61(7), to permit the deceased spouse's interest to pass by will to others.

To summarize, the drafter should ascertain which—if any—of the special rules of chapter 766 the spouses wish to apply to the marital property regime they are creating by contract. The spouses can spell out their intent either in the agreement's definition of marital property or in specific provisions addressing each special rule. Arguably, a bare reference to classifying assets "as marital property" or "as marital property under chapter 766 of the Wisconsin Statutes" creates ambiguities as to whether all, some, or none of the special rules are to be applied, although section 766.58(7) makes it clear that the terminable interest rule of section 766.62(5) and the frozen interest rule of section 766.61(7) will apply unless specifically negated. A number of drafting options are set forth in the sample marital property agreement to classify all or most of the spouses' assets as marital property. *See infra* § 7.151.

#### **4. Limited Marital Property Agreements with Respect to Specific Assets or Liabilities [§ 7.116]**

A review of the comments to UMPA sections 3 and 10 reveals that limited marital property agreements are contemplated by the Act. The UMPA section 10 comment presupposes that a marital property agreement usually will be a postmarital agreement and that “the approach in this Act [UMPA] toward marital property agreements is that there may, and usually will, be many of them made at numerous times during a marriage.” A limited marital property agreement is one executed by the spouses (or by persons intending to marry) for limited purposes such as determining the ownership rights to certain defined assets, establishing responsibility for certain defined liabilities, or dealing with other selected economic issues in their marriage.

Amendments to section 766.58(6) by the 1985 Trailer Bill support the view that more relaxed financial-disclosure standards may be applied to limited marital property agreements under the Act. Section 766.58(6)(c) originally required “fair and reasonable disclosure” as a condition of enforceability. The 1985 Trailer Bill substituted the more lenient standard of “fair and reasonable disclosure, *under the circumstances*” (emphasis added). This change suggests that when relatively small property rights or economic incidents are involved, the courts may determine that no disclosure is necessary. *See* Wis. Stat. Ann. § 766.58 Legis. Council Notes—1985 Act 37, §§ 112–121 (West 2009).

The state of Washington has held that “property status agreements,” much like Wisconsin’s limited marital property agreements, are enforceable in a divorce proceeding, even though originally prepared for estate planning purposes. *See Hadley v. Hadley*, 565 P.2d 790, 793 (Wash. 1977). It is not clear whether this approach will be followed in Wisconsin. In *Levy v. Levy*, 130 Wis. 2d 523, 388 N.W.2d 170 (1986), the Wisconsin Supreme Court held that a comprehensive pre-Act marriage agreement, which by its terms was to apply in the event of death but was silent on the question of divorce, could not be relied on by the circuit court under section 767.255(11) (now section 767.61(3)(L)) in arriving at a divorce property division. The better drafting practice is to carefully spell out the intended applicability of a limited marital property agreement, rather than to leave the issue to the vicissitudes of judicial determination.

Chapter 10, *infra*, discusses the issues involved in using limited marital property agreements to reclassify (1) a nongrantor spouse's interest in property used to pay premiums on life insurance policies held by an irrevocable life insurance trust to which employment-related or other life insurance policies have been assigned, or (2) the ownership interest or proceeds of the policies themselves without regard to the classification of the property used to pay the premiums.

A sample limited marital property agreement is set forth in section 7.157, *infra*.

## **5. Marital Property Agreements Permitting Reclassification by Unilateral Action of One Spouse [§ 7.117]**

Marital property agreements that permit either spouse, acting alone, to cause a change in classification of property may be a useful estate planning device. For example, such an agreement might provide that the spouses' property is individual property based on a classification mechanism spelled out in the agreement, but that either spouse may by written notice to the other cause future property acquisitions to be classified as they otherwise would be under the Act; property acquired before notice of the change was received would remain classified under the agreement's terms in much the same fashion as under the statutory terminable property classification agreements in sections 766.588 and 766.589. Alternatively, the agreement might allow the notice to operate retroactively, in effect causing any property classifications under the agreement to fall away completely, thereby reclassifying all property as if there had been no agreement. In addition, after the death of one of the spouses, either type of agreement might (1) grant the survivor a limited time in which to change property classifications to those the property would have had under the Act, or (2) provide the survivor with certain elective rights against the deceased spouse's estate similar to those he or she would have had under the Act.

Agreements permitting unilateral reclassification of property are attractive to drafters, particularly in the case of stable marriages in which there is a considerable disparity in the spouses' relative wealth or earnings potential but neither spouse is likely to exercise the right to change classifications. Such agreements may permit a single attorney to

represent both spouses with less risk of running afoul of the ethical concerns discussed in chapter 14, *infra*. Incorporating provisions for unilateral reclassification may also eliminate the need for detailed financial disclosures and avoid a confrontational atmosphere in developing a marital property agreement that permits the spouses' existing estate planning objectives to remain intact.

It is beyond the scope of this discussion to suggest the exact form or content of such agreements. Drafters should, however, be aware of several practical considerations. First, the drafter must overcome the section 766.58(4) requirement that a marital property agreement can be amended or revoked only by a later marital property agreement—which requires execution by both spouses. Wis. Stat. § 766.58(1), (4); *see supra* § 7.23. This obstacle could be overcome by structuring the agreement so that the unilateral action of one spouse constitutes an action pursuant to and in effectuation of the agreement, rather than an amendment or revocation. Basically, the spouses would agree that either of them, acting alone, could take certain actions. That would be the essence of the agreement itself. The Act grants spouses great contractual freedom to vary its provisions. Wis. Stat. § 766.17. It should even be possible for the spouses to contractually agree that either of them may take actions tantamount to amendment or revocation because subsections 766.58(1) and (4) are not among the designated statutory provisions that cannot be varied by a marital property agreement. *See supra* §§ 7.7–.14, .22–.24.

The drafter of an agreement permitting one spouse to unilaterally change property classifications must also be careful that the agreement has sufficient substance so that it is not subject to attack as being illusory. *See* 1 Farnsworth, *supra* § 7.50, § 2.13; *see also* Restatement (Second) of Contracts § 77 cmt. a, § 2 cmt. e (1981). This objective might be accomplished by including provisions at variance with the Act that are sufficient to provide substance. In this regard, it is important to remember that the Act specifically states that marital property agreements do not require consideration to be enforceable. Wis. Stat. § 766.58(1); *see supra* § 7.20.

Finally, careful consideration should be given to the practical and theoretical problems associated with the retroactive reclassification of property by the action of one spouse. What are the tax consequences, if any, of the right of one spouse to unilaterally classify or reclassify property? What effect will such agreements have on obligations to

creditors who have actual knowledge of the agreement or are provided with a copy? Notwithstanding these uncertainties, it can be expected that creative planners will find uses for agreements that permit the unilateral actions of one spouse to affect the classification of property.

A sample of a marital property agreement permitting reclassification by the unilateral action of one spouse is set forth in section 7.160, *infra*.

## **6. Desirability of Retitling Assets Reclassified by Marital Property Agreement [§ 7.118]**

One consideration ancillary to the preparation of a marital property agreement is whether it is necessary or desirable to execute new documents of title for assets reclassified by the agreement. Section 766.31(10), which specifically permits the spouses to reclassify their property by marital property agreement, seems clear authority for the proposition that the agreement alone suffices to determine the ownership of assets.

A marital property agreement may also provide for survivorship, either as a right of management and control under section 766.58(3)(b) or as a right to dispose of any property of either or both of the spouses upon death under section 766.58(3)(c). The survivorship feature in a marital property agreement should similarly control at the death of one of the spouses even though documents of title to assets held by either or both of the spouses are not changed.

If a marital property agreement reclassifies assets, or adds a survivorship feature to certain assets, execution of new documents of title may be a matter of convenience, particularly when the title is a matter of public record and there is reason to have the public record reflect the realities of ownership or the form of holding. Retitling assets also may simplify the personal representative's task following the death of one of the spouses.

Joint bank accounts under chapter 705 and joint brokerage account agreements present some difficult problems. *See infra* ch. 10. Even though a marital property agreement classifies the assets held in such accounts as marital property without a right of survivorship, it is likely that survivorship provisions in the account agreement will effectively control disposition of the assets in the account at death as between the



financial institution or brokerage and the person designated as survivor. In the case of joint bank accounts, the result is governed by section 705.04(1), which states that sums remaining on deposit at the death of a party to a joint account belong to the survivor as against the estate of the decedent unless there is clear and convincing evidence of a different intention at the time the account is created. Normally there will be no such evidence available for joint accounts already in existence at the time the marital property agreement is executed, but the agreement itself may constitute such evidence for joint accounts created after the execution of the agreement.

In the case of joint brokerage accounts, the survivorship feature is a matter of contract and may be regarded as a nonprobate transfer on death under sections 705.10 or 705.21–.31, with the survivorship feature given priority over any conflicting treatment in a marital property agreement. In any event, the treatment and disposition of joint bank accounts and joint brokerage accounts should be specifically addressed in the spouses' marital property agreement. *See, e.g.*, part A. of Article I of the marital property agreement form at section 7.151, *infra*. If it is inconsistent with the purposes of their marital property agreement (or would create undesired results under their estate plan), the spouses should be counseled to change existing accounts into a form of co-ownership without survivorship and to avoid establishing financial institution or brokerage accounts with a survivorship feature in the future.

#### **IV. Marriage Agreements Not Governed by the Act** **[§ 7.119]**

##### **A. In General [§ 7.120]**

Marriage agreements not governed by the Act fall into three major categories:

1. Marriage agreements executed before the Act's adoption on April 4, 1984;
2. Marriage agreements executed between the Act's adoption on April 4, 1984, and the Act's effective date of January 1, 1986, that the spouses did not intend to treat as anticipatory marital property agreements, *see supra* § 7.26; and

3. Marriage agreements executed by nonresidents either before or after the Act's effective date on January 1, 1986, but before the spouses' determination date occurs through establishment of their domicile in Wisconsin.

➤ **Note.** Attorneys often refer to marriage agreements in each of these three categories as “predetermination date marriage agreements.” Under the Act, the determination date is the last to occur of the following: (1) marriage; (2) the date both spouses are domiciled in Wisconsin; or (3) January 1, 1986. Wis. Stat. § 766.01(5). Thus, the universe of predetermination date marriage agreements is a broad one, encompassing not only these three types of agreements, but also marital property agreements executed by persons intending to marry, *see supra* § 7.25, and anticipatory marital property agreements executed by spouses or unmarried persons who subsequently marry each other, *see supra* § 7.26. In other words, the term predetermination date marriage agreement can refer to certain types of marital property agreements under the Act as well as to certain types of marriage agreements not governed by the Act. Because the discussion in sections 7.121–147, *infra*, pertains exclusively to marriage agreements not governed by the Act, the term predetermination date marriage agreement is not used to refer to these agreements.

Marriage agreements in the first two categories above are hereinafter referred to as “pre-Act marriage agreements”; they are discussed in sections 7.121–146, *infra*. Marriage agreements in the third category are discussed in section 7.147, *infra*, and should be distinguished from anticipatory marital property agreements executed by nonresident spouses or spouses-to-be before establishing their domicile in Wisconsin, *see supra* § 7.26.

## **B. Saving Provisions Under the Act [§ 7.121]**

The Act contains several saving provisions designed to avoid the impairment of marriage agreements entered into before the determination date and not intended to be governed by the Act. The first is found in section 766.58(12)(a), which provides that chapter 766 does not affect any provision in a “document” that (1) is signed before the determination date by spouses or by unmarried persons who subsequently marry each other, (2) affects the property of either of them, and (3) is enforceable by

either of them without reference to chapter 766, unless the spouses provide otherwise in a marital property agreement made after the determination date. The term *document* is broad and is clearly intended to cover marriage agreements as well as other types of contracts between the spouses. Section 766.58(12)(a) is based on UMPA section 10(j). The comment to UMPA section 10 indicates that this provision is designed to avoid retroactivity and the resulting impairment of contractual obligations: “Thus a predetermination date agreement dealing with subject matter such as that in [UMPA] will simply continue to stand on such authority as it had without [UMPA], and [UMPA] neither helps nor hinders that agreement.” UMPA § 10 cmt.

The second saving provision, section 766.58(12)(b), builds on the first. It was added by the 1985 Trailer Bill for the specific purpose of recognizing the enforceability after the determination date of provisions in marriage agreements executed before the determination date, which provisions are intended to negate, apply, or modify any right or obligation that might accrue under the Act or under any other community property system. Section 766.58(12)(b) indicates that the provision (or amendment to a provision) is enforceable after the determination date if the document of which it is part was otherwise enforceable when executed.

The statute provides a choice of enforceability standards for marriage agreements (or amendments to such agreements) executed after April 4, 1984 (the date 1983 Wisconsin Act 186 was signed by the governor), and before the determination date. The party seeking to enforce the provision (or amendment) is entitled to enforcement if the underlying document either (1) met the legal standards for enforceability applicable when it was executed or (2) would have met the enforceability standards applicable under section 766.58 had it been executed after the determination date. *See* Wis. Stat. Ann. § 766.58 Legis. Council Comm. Supplemental Notes Relating to 1985 Act 37 (West 2009). Thus, the standards of the Act can be used to judge the enforceability of some marriage agreements (or amendments to agreements) entered into after the Act was signed into law but before the spouses’ determination date. This provision also appears to apply to marriage agreements executed by nonresident spouses before they become domiciled in Wisconsin. *See infra* § 7.147. Adopting a dual test for enforceability permits the party seeking enforcement to satisfy whichever standard of enforceability is easier.

During the years when the legislature was debating adoption of a system of marital property based on community property, couples were entering into marriage agreements designed to negate or modify the applicability of community property generally or of marital property based on community property concepts in particular. The section 766.58(12)(b) saving provision probably was included in the 1985 Trailer Bill in recognition of this fact. Pursuant to section 766.58(12)(b), provisions of that type are enforceable if the agreement of which they are part is also enforceable.

A final provision, section 766.58(12)(c), states that the saving provisions of section 766.58(12) do not affect anticipatory marital property agreements executed under section 766.585, *see supra* § 7.26.

To summarize, section 766.58(12) provides that a marriage agreement entered into before the determination date by spouses or unmarried persons who subsequently married each other, and not modified after the determination date by a marital property agreement governed by chapter 766, continues to be judged under pre-Act common law and statutory standards. Further, any provision or amendment to a provision in such a marriage agreement, which provision or amendment is intended to negate, apply, or modify rights or obligations acquired under the Act or under a community property system, continues to be enforceable after the determination date; enforceability is contingent, however, on whether the provision or amendment either was enforceable when the agreement was executed or would be enforceable under the Act. Because of these saving provisions, an understanding of the requirements of prior law is necessary in assessing the enforceability of such agreements under the Act.

## **C. Requirements for Pre-Act Marriage Agreements Intended to Be Enforceable at Death [§ 7.122]**

### **1. In General [§ 7.123]**

Wisconsin has a relatively well-developed body of pre-Act law dealing with premarital and postmarital agreements. A valid marriage agreement enforceable at the death of one of the spouses under pre-Act law must meet all the following substantive and procedural requirements:

1. It must be in writing and signed by the party sought to be bound.
2. It must either make reasonable provision for a party who is giving up substantial rights or, alternatively, involve full and fair disclosure by both parties.
3. It must provide sufficient consideration to support the agreement, which requirement will usually be satisfied if one of the alternative conditions in item 2, above, is met.
4. It must be free from any taint of overreaching or fraud.

It should be noted that the first requirement is based on either section 241.02 (1983–84) or section 861.07(1) (1983–84); the second, third, and fourth requirements derive from court decisions involving the enforceability of marriage agreements at death.

No reported Wisconsin decision has been found in which a premarital or postmarital marriage agreement was held invalid under pre-Act law following the death of one of the spouses. In fact, the supreme court repeatedly stated that it regarded such agreements with favor. *See Koeffler v. Koeffler*, 215 Wis. 115, 123, 254 N.W. 363 (1934); *Bibelhausen v. Bibelhausen*, 159 Wis. 365, 373, 150 N.W. 516 (1915); *Oesau v. Estate of Oesau*, 157 Wis. 255, 259, 147 N.W. 62 (1914).

If the agreement is also to be enforceable as a property settlement agreement in the event of the parties' divorce, it must be in writing and must be equitable as to both parties. These latter requirements are statutory. *See* Wis. Stat. § 767.61(3)(L); *see also infra* §§ 7.133–.140.

## **2. Statute of Frauds [§ 7.124]**

A marriage agreement that is to be enforceable at death under pre-Act law must be in writing. Section 241.02(1) is the Wisconsin counterpart of the original English statute of frauds. The statute provides that certain agreements are void (not merely voidable or unenforceable) unless the agreement, or some note or memorandum expressing the consideration, is reduced to writing and signed by the party to be charged. Under section 241.02(1)(c), agreements made upon consideration of marriage, except mutual promises to marry, are subject to the statute's provisions.

The Act made section 241.02(1) inapplicable to marital property agreements complying with chapter 766. *See* Wis. Stat. § 241.02(2). The net effect of the statutory change is to substitute the section 766.58(1) requirements governing marital property agreements for the requirements of section 241.02(1)(c). *See supra* §§ 7.17–.21. The section 766.58(1) requirements apply to all marital property agreements entered into after the determination date, to marital property agreements executed before marriage, *see supra* § 7.25, and to anticipatory marital property agreements under section 766.585, *see supra* § 7.26. They also may apply to marriage agreements entered into between the enactment of the Act and the determination date. *See supra* § 7.121.

In addition to the general statute of frauds contained in section 241.02(1)(c), the statutes formerly provided that the surviving spouse's right to elect against the decedent's will could be barred by the terms of a written agreement signed by both spouses. *See* Wis. Stat. § 861.07(1) (1983–84). Such an agreement might be entered into before or after marriage. This provision was repealed as of the Act's effective date (January 1, 1986), along with the other statutory provisions relating to spousal elective rights. However, for pre-Act marriage agreements, former section 861.07(1) effectively requires that marriage agreements intended to apply at death be reduced to a signed writing.

### **3. Doctrine of Partial or Full Performance [§ 7.125]**

Assuming that a pre-Act marriage agreement is not reduced to writing, does the equitable doctrine of partial or full performance operate to take it out of the statute of frauds? The doctrine of partial or full performance evolved to cover situations in which an oral contract subject to the statute of frauds was partially or wholly performed. The policy behind the doctrine is to avoid an injustice by enforcing a contract when the parties' conduct evidences substantial reliance on the contract's existence. One Wisconsin decision, *Rowell v. Barber*, 142 Wis. 304, 125 N.W. 937 (1910), has considered this question. Although the Wisconsin Supreme Court referred to the well-recognized doctrine that a contract void under the statute of frauds is enforceable if fully executed, it held that no full performance of the agreement was at issue. The oral premarital agreement, being void by the statute's express provision, was not made valid by the subsequent execution of a postmarital agreement incorporating its terms. (This part of the holding can be best understood in light of the then prevailing judicial attitude that postmarital

agreements were invalid either as a matter of public policy or for want of consideration.) In addition, the court held that neither the act of marriage nor the husband's furnishing of support and maintenance was sufficient part performance to take the agreement out of the statute of frauds. Further, the court noted that no property was transferred during the spouses' lifetime pursuant to the agreement. *Id.* at 316–17.

This holding is generally consistent with the majority view on what constitutes sufficient performance to render an oral premarital agreement enforceable. See R.D. Hursh, Annotation, *What Constitutes Past Performance Sufficient to Take Agreement in Consideration of Marriage out of Statute of Frauds*, 30 A.L.R.2d 1419 (1953). The test is stringently applied and is ordinarily reserved for situations in which the conduct of the spouse seeking to establish the marriage agreement cannot be explained in the absence of the existence of a contract. See *Rossiter v. Rossiter*, 666 P.2d 617 (Haw. Ct. App. 1983). In practice, the test may be virtually impossible to meet. See 2 Lindey & Parley, *supra* § 7.21, § 110.64[2]. For a more contemporary treatment of this issue, see *Hall v. Hall*, 271 Cal. Rptr. 773 (Ct. App. 1990) (finding oral agreement enforceable), discussed *supra* § 7.27.

#### **4. Reasonable Provision for Spouse Versus Adequate Disclosure [§ 7.126]**

The Wisconsin Supreme Court historically employed a two-pronged test in examining pre-Act premarital and postmarital property settlement agreements intended to be enforceable at death. Either reasonable provision must have been made for a spouse who surrendered significant rights or the spouses must have fully and fairly disclosed their net worths to each other. See *Madison Bank & Trust v. Beat (In re Estate of Beat)*, 25 Wis. 2d 315, 321, 130 N.W.2d 739 (1964); *Knippel v. Marshall & Ilsley Bank (In re Estate of Knippel)*, 7 Wis. 2d 335, 345–46, 96 N.W.2d 514 (1959); *Bibelhausen v. Bibelhausen*, 159 Wis. 365, 383, 150 N.W. 516 (1915).

Although the court has stopped short of requiring full and fair disclosure as an absolute condition for a valid pre-Act marriage agreement enforceable at death, it has noted that such a broad rule might be applicable in situations in which one of the spouses was young or inexperienced. See *Koeffler v. Koeffler*, 215 Wis. 115, 127, 254 N.W. 363 (1934). Moreover, the equitableness test of section 767.61(3)(L),

which applies if the agreement is to be enforceable at dissolution, requires fair and reasonable disclosure. *See Button v. Button*, 131 Wis. 2d 84, 388 N.W.2d 546 (1986); *infra* §§ 7.133–.140. Consequently, attorneys drafting comprehensive marriage agreements before the effective date of the Act normally recommended full disclosure of assets and liabilities by both parties, as well as a reasonable provision for the spouse having the significantly smaller estate.

A number of authorities have pointed out that because the purpose of disclosure is to prevent overreaching, whenever a party waiving valuable rights under a marriage agreement has independent knowledge of the general nature of the property and income of his or her spouse or intended spouse, the knowledge serves as a substitute for disclosure. The spouse with independent knowledge cannot later repudiate the agreement even though the provision made is disproportionate to the value of the rights given up. *See* 2 Lindey & Parley, *supra* § 7.21, §§ 110.68[5], 120.56[2]; *see also Del Vecchio v. Del Vecchio*, 143 So. 2d 17 (Fla. 1962); *Cox v. West (In re Estate of West)*, 402 P.2d 117 (Kan. 1965); *Hartz v. Hartz*, 234 A.2d 865, 870–71 (Md. 1967); *In re Marriage of Coward*, 582 P.2d 834 (Or. Ct. App. 1978). This concept has found its way into the Act. *See* Wis. Stat. § 766.58(6)(c)2. In the context of pre-Act marriage agreements enforceable at dissolution, the Wisconsin Supreme Court has held that independent knowledge serves as a substitute for disclosure. *Button*, 131 Wis. 2d at 95. However, a general or imputed knowledge will not suffice. *Schumacher v. Schumacher*, 131 Wis. 2d 332, 338, 388 N.W.2d 912 (1986).

Some of the difficulties created by arguably inadequate provisions or a failure to disclose are illustrated by *Estate of Campbell v. Chaney*, 169 Wis. 2d 399, 485 N.W.2d 421 (Ct. App. 1992). In early 1985, the husband's attorneys drafted a premarital agreement. The agreement contained no financial disclosures and was apparently unaccompanied by any disclosure of financial information by the parties. The husband's estate at the time was in the \$6–8 million range, and the premarital agreement provided the wife-to-be with a fixed payment of \$500,000 in the event of the husband's death.

At the suggestion of one of the husband's attorneys, before signing the agreement, the wife-to-be consulted with an independent attorney, who recommended that she not sign it, because (1) it would be inequitable, (2) there was insufficient financial disclosure, and (3) he needed more time to review the agreement. Despite this



recommendation, the wife-to-be signed the agreement before the marriage.

Following the husband's death, the wife challenged the agreement on grounds of duress, undue influence, breach of contract, misrepresentation, inadequate provision, and inadequate financial disclosure. The personal representative of the estate ultimately reached a \$1 million settlement with the wife and then commenced a negligence action against the husband's attorneys. The court held that to establish that the defendant attorneys were negligent, the estate would have to first prove that they breached the standard of professional care in drafting the premarital agreement. If a document is attacked in litigation, but the attorneys were not negligent in preparing it, they cannot be held liable. *Id.* at 409. Secondly, the estate would have to establish causation, i.e., that the attorneys' negligence caused "weakness" in the premarital agreement and that the weakness caused the litigation by and with the widow. *Id.* To recover the difference between the settlement and the payment required to be made to the widow under the premarital agreement, the husband's estate needed to prove that the weakness of the agreement caused its decision to settle, and that no other causal factors were at work. *Id.* at 409–10. In addition, the husband's estate needed to show that the settlement was reasonable and made in good faith. *Id.* at 410.

However, the court went on to say that an attorney's negligence does not strictly depend on whether the premarital agreement can be enforced:

If an attorney drafts a prenuptial agreement without attaching a financial statement, the fact-finder could conclude that the attorney failed to use reasonable care, that is, that the attorney was negligent. It is immaterial that the agreement might later be enforced after a finding that the widow already knew the financial information. The fact-finder could still find that the attorney failed to exercise reasonable care in drafting the agreement. If that failure caused the estate to settle a claim that a proper agreement would have made meritless, then the attorney may be held liable.

*Id.*

➤ **Comment.** The failure to attach a financial statement to a premarital agreement is not necessarily evidence of negligence. There is no authority that physical attachment of financial disclosures was ever a requirement for enforceability of premarital property

settlement agreements before the effective date of the Act. Clearly physical attachment is not required under the Act. To avoid enforcement, section 766.58(6)(c) requires that the spouse against whom enforcement is sought prove that *before execution* he or she did not receive fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations, and did not have notice (i.e., actual knowledge) of the other spouse's property or financial obligations. *See supra* § 7.48. Thus, the appearance in Wisconsin jurisprudence of a purported requirement of attaching financial statements to pre-Act marriage agreements (as opposed to providing fair and reasonable financial disclosures) is troubling, because it appears to be much narrower than the requirements that had evolved under pre-Act case law or those under the specific provisions of section 766.58(6)(c).

The question of the reasonableness of a provision for a spouse usually arises only if there was a failure to make full disclosure and the affected spouse did not have independent knowledge. *See Knippel*, 7 Wis. 2d at 345–46. Some of the factors cited by Lindey & Parley, *supra* § 7.21, for determining the fairness and reasonableness of a provision are the following:

1. The parties' circumstances when the agreement was made;
2. The parties' ages;
3. The parties' stations in life and standards of living;
4. The parties' assets and income;
5. The parties' vocations and employment;
6. The parties' health;
7. The parties' family relationships (specifically, whether they have any children); and
8. The parties' conduct after the marriage (shedding light on whether the parties understood the terms of the agreement).

2 Lindey & Parley, *supra* § 7.21, § 110.66[1].

It has been held that the reasonableness of a provision for a spouse is to be weighed at the time of the agreement's execution. *See Spector v. Spector*, 531 P.2d 176, 185 (Ariz. Ct. App. 1975); *Del Vecchio*, 143 So. 2d at 19–20; *In re Kaufmann's Estate*, 171 A.2d 48 (Pa. 1961).

In cases involving the termination of the marriage by death, a marriage agreement will not be substantively reviewed at the time of death, even when the circumstances of one of the spouses materially changed for the better, if the agreement was fair and the parties understood its intent at the time of execution. *See Bibelhausen*, 159 Wis. at 372, 378.

## **5. Adequate Consideration [§ 7.127]**

Virtually all adjudicated Wisconsin cases dealing with pre-Act marriage agreements enforceable at death have involved nondisclosure. In addition, many have involved what appeared to be unreasonable provisions for a spouse who gave up significant rights. The absence of independent counsel for the less-propertied spouse has been another common thread. The Wisconsin Supreme Court has therefore often found it necessary to examine the adequacy of the consideration and the overall fairness of the agreement.

The court has not adopted a formal framework for determining the adequacy of consideration in pre-Act marriage agreements, observing that a small amount may be enough if agreed on by the parties. *See Nickolay v. Nickolay's Estate*, 249 Wis. 571, 575, 25 N.W.2d 451 (1946); *Bibelhausen*, 159 Wis. at 376–77. The court has said that manifestly unfair and unreasonable consideration is tantamount to fraud. *Bibelhausen*, 159 Wis. at 383–84. It should be noted that cases like *Estate of Nickolay* and *Bibelhausen* arose at a time when property settlement provisions applicable at divorce were not permitted, and marriage agreements for the most part were confined to property arrangements at death. However, it would be inaccurate to infer from this fact that only property arrangements applicable at death should be looked to in determining the adequacy of consideration. In fact, the provisions of the marriage agreement as a whole must be evaluated.

The test for adequacy of consideration in premarital agreements has differed historically from the test in postmarital agreements. In the former, it has been stated that “marriage itself, under some circumstances

at least, is a sufficient consideration to support the contract.” *Bibelhausen*, 159 Wis. at 383. Cases from other jurisdictions confirm this view. See *Barnhill v. Barnhill*, 386 So. 2d 749, 751 (Ala. Civ. App. 1980); *Eule v. Eule*, 320 N.E.2d 506, 509 (Ill. App. Ct. 1974); *Friedlander v. Friedlander*, 494 P.2d 208, 212 (Wash. 1972) (stating that marriage is consideration of highest value to support premarital agreement). Accordingly, if a premarital agreement recites the mutual promises to marry and the marriage is subsequently performed, there will be valid consideration for the agreement. *Williams v. Williams*, 569 S.W.2d 867, 871 (Tex. 1978).

In the postmarital context, the mutual release of rights in each other’s solely owned property has been deemed sufficient consideration to support the agreement. *Beat*, 25 Wis. 2d at 325–26; *Nickolay*, 249 Wis. at 574–75.

Section 861.07(1) (1983–84) permitted a written agreement signed by the spouses to bar the surviving spouse’s right to elect against the decedent’s will. The comment to Wisconsin Statutes Annotated section 861.07(1) (West 1971) indicates that consideration for such an agreement would be necessary “to prevent overreaching by a dominant spouse.” Although this statutory provision was repealed by the Act, it states the applicable rule for pre-Act marriage agreements that seek to bar spousal elective rights.

The foregoing cases support the conclusion that a written premarital agreement, executed before the effective date of the Act and accompanied by full disclosures of net worth by both parties, stands on the sufficiency of the parties’ mutual promises to marry even if no special financial provision is made for either party. A written postmarital agreement, again accompanied by full disclosures, stands on the consideration of the mutual releases of the parties’ rights in each other’s property. In either case, the agreement might still fail if procured by misrepresentation, undue influence, duress, or fraud. Absent those, its validity should be recognized at the time of death of one of the parties. See sections 7.133–.140, *infra*, regarding the considerations that apply if enforcement of the agreement is sought when a marriage dissolves.

## 6. Fairness [§ 7.128]

Judicial scrutiny of pre-Act marriage agreements that are contested following a spouse's death ordinarily has concluded with an examination for "fairness." At its heart, this is an examination for unconscionability, overreaching, and fraud at the time the agreement was entered into. In Wisconsin, the fairness test has been lumped together with a review of the adequacy of consideration. See *Bibelhausen*, 159 Wis. at 383–84. As discussed in sections 7.41–46, *supra*, the requirement that a marriage agreement not be unconscionable when made is also very much a part of the enforceability provisions for marital property agreements under the Act.

The *Bibelhausen* case indicated that in applying the fairness test, the circumstances surrounding the execution of the marriage agreement would be reviewed, but if the provisions were fair, the circumstances that existed when one of the parties died would not. *Id.* at 384–86. This is in contrast to the Wisconsin cases dealing with the substantive fairness of an agreement at divorce, discussed in sections 7.135–.140, *infra*. Other courts have also held that changed circumstances at death will not be considered in enforcing a marriage agreement at death. See, e.g., *Martin v. Farber*, 510 A.2d 608, 610 (Md. Ct. Spec. App. 1986); *In re Estate of Youngblood v. Youngblood*, 457 S.W. 2d 750, 756 (Mo. 1970). See also the more detailed treatment of this subject in June Miller Weisberger, *Spousal Property Agreements: An Evolving Concept in Wisconsin and Elsewhere*, 5 Wis. Women's L.J. 43, 61–62 (1990).

Courts in other jurisdictions have held, in reviewing the validity of a premarital agreement, that it is not absolutely necessary for a spouse giving up significant rights to be represented by independent counsel, particularly when that spouse was reasonably knowledgeable and understood the agreement or was aware of his or her right to independent counsel but chose not to obtain counsel. See *Newman v. Newman*, 653 P.2d 728, 733 (Colo. 1982); *Pniewski v. Przybysz*, 183 N.E.2d 437 (Ohio Ct. App. 1962); *McFerron v. Trask*, 472 P.2d 847, 849–50 (Or. Ct. App. 1970); *In re Marriage of Cohn*, 569 P.2d 79 (Wash. Ct. App. 1977); see also *Frey v. Frey*, 471 A.2d 705, 711 (Md. 1984) (emphasizing importance of independent legal advice in evaluating whether agreement was voluntarily and understandingly made); *Braddock v. Braddock*, 542 P.2d 1060, 1062–63 (Nev. 1975) (applying Ohio law to agreement executed there and holding that agreement was not void for lack of independent counsel, provided that it was voluntarily and

understandingly made). *But see Counts v. Benker (In re Estate of Benker)*, 331 N.W.2d 193 (Mich. 1982) (failure to have independent counsel along with failure to discuss or disclose assets vitiated agreement).

In none of the Wisconsin Supreme Court cases involving the enforceability of a pre-Act marriage agreement at death is there any evidence that the person in the inferior bargaining position was independently represented by counsel when the marriage agreement was entered into, nor is there any intimation in those cases that such representation is either a legal requirement or an ethical duty. However, the very fact that the aggrieved spouse in these contested Wisconsin marriage agreement cases was *not* independently represented by counsel should serve as a warning.

In sum, a pre-Act marriage agreement should not be regarded as *prima facie* unfair merely because a spouse or a person intending to marry agreed that he or she would receive no financial provision, particularly if that person received full and fair disclosure, had adequate time to consider the agreement, and had the advice of independent counsel. With respect to ethical considerations, see chapter 14, *infra*.

## **7. Construction and Enforceability [§ 7.129]**

Marriage agreements are governed by the same rules of construction that apply to other contracts. The basic purpose is to effect the intent of the parties. If an agreement is clear and unambiguous, neither construction nor resort to parol evidence is necessary. *See Luedtke v. Luedtke*, 65 Wis. 2d 387, 392–93, 222 N.W.2d 643 (1974); *First Nat'l Bank v. Harris (In re Estate of Harris)*, 7 Wis. 2d 417, 420–21, 96 N.W.2d 718 (1959); *Oesau v. Estate of Oesau*, 157 Wis. 255, 261–62, 147 N.W. 62 (1914).

The burden of impeaching a pre-Act marriage agreement that is enforceable at death falls on the party asserting the invalidity. *Oesau*, 157 Wis. at 259. A presumption of fraud arises once that party demonstrates that there was neither a full and fair disclosure of the spouses' net worth nor an obviously reasonable and adequate provision for a spouse surrendering significant rights under the terms of the agreement. *See Beat*, 25 Wis. 2d at 321; *Knippel*, 7 Wis. 2d 335 at 345–46. The party defending the agreement's validity then has the burden of

introducing evidence to rebut the presumption. A general discussion of the burden of proof is found in 2 Lindey & Parley, *supra* § 7.21, § 110.71.

## **8. Modification and Rescission [§ 7.130]**

Marriage agreements, like other contracts, may be modified or revoked by the mutual consent of the parties, provided that the intent to do so is clear and proven by a preponderance of the evidence. *See Dalgarn v. Leonard*, 87 N.E.2d 728 (Ohio Prob. Ct. 1948), *aff'd*, 90 N.E.2d 159 (Ohio Ct. App. 1949). No Wisconsin decisions have been found on oral modification or revocation of marriage agreements; presumably, modification or revocation must be accomplished in writing. Oral rescissions are to be avoided. *See, e.g., Masterson v. Masterson*, 139 S.W.2d 30 (Ark. 1940) (holding that alleged oral rescission not accompanied by physical destruction of agreement was ineffective).

## **9. Conflict of Laws [§ 7.131]**

For a discussion of the application of conflict-of-laws principles to marriage agreements, see chapter 13, *infra*.

## **D. Subject Matter of Pre-Act Marriage Agreements [§ 7.132]**

The subject matter of pre-Act marriage agreements intended to be enforceable at death could include the identification, variance, or relinquishment of rights and interests that the spouses or intended spouses would otherwise acquire in each other's property and estates by reason of the marriage. For example, the spouses could release their distributive shares in each other's estates; the wife could bar her dower and the husband his curtesy; or they could surrender their respective rights of election to take against each other's estates. Either of them could transfer money or property or both to the other, either before the marriage or afterward.

Nearly all reported Wisconsin cases dealing with pre-Act property settlement agreements have involved a wife giving up either dower rights or statutory elective rights in lieu of dower. *See Beat*, 25 Wis. 2d 315;

*Koeffler v. Koeffler*, 215 Wis. 115, 254 N.W. 363 (1934); *Bibelhausen*, 159 Wis. 365. In some cases, both spouses have given up such rights. See *Beat*, 25 Wis. 2d 315; *Nickolay*, 249 Wis. 571; *Oesau*, 157 Wis. 255.

See sections 7.133–140, *infra*, for a discussion of Wisconsin cases involving pre-Act marriage agreements containing provisions intended to be enforceable in the event of dissolution of the marriage.

A pre-Act marriage agreement can apply to property acquired after its execution. See *Cortte v. Tolzman (In re Estate of Cortte)*, 230 Wis. 103, 107, 283 N.W. 336 (1939). A release of all rights that arise by law in a spouse's estate has been held sufficient to bar statutory allowances. See *Deller v. Deller*, 141 Wis. 255, 124 N.W. 278 (1910). By way of contrast, in *Beat*, 25 Wis. 2d at 330–31, the court held that an agreement containing mutual releases of rights to the spouses' property owned "at the time of their marriage" was to be distinguished from one containing a release of the deceased spouse's estate (including subsequently acquired property). While the latter would bar the surviving spouse from claiming a widow's allowance as in *Deller*, the former did not. One must assume that the decedent spouse in *Beat* in fact owned additional, subsequently acquired property at death sufficient to support the allowance.

The Wisconsin Supreme Court has also held that execution of a will making a more generous provision for a spouse than required by the marriage agreement neither bars the spouse from accepting the testamentary provision nor invalidates the agreement. *Jones v. First Nat'l Bank & Trust Co. (In re Will of Paulson)*, 254 Wis. 258, 36 N.W.2d 95 (1949); see also *Greiling v. Genz (In re Will of Greiling)*, 264 Wis. 146, 59 N.W.2d 241 (1953).

Several community property jurisdictions have held that community property interests can be prospectively abrogated or reclassified by marriage agreement. See *Spector v. Spector*, 531 P.2d 176 (Ariz. Ct. App. 1975); *Sarpy v. Sarpy*, 323 So. 2d 851 (La. Ct. App. 1975); *Huff v. Huff*, 554 S.W.2d 841 (Tex. Civ. App. 1977). These holdings are consistent with the broad contractual freedom under section 766.17(1) to vary the Act's property law system. See *supra* § 7.6.



## **E. Requirements for Pre-Act Marriage Agreements Intended to Be Enforceable at Dissolution of Marriage [§ 7.133]**

### **1. In General [§ 7.134]**

Historically, the courts in Wisconsin and elsewhere held that provisions in marriage agreements that tended to limit a spouse's liability with respect to support, maintenance, or property settlement arrangements in the event of separation or divorce were void as being contrary to public policy. See *Kunde v. Kunde*, 52 Wis. 2d 559, 191 N.W.2d 41 (1971); *Caldwell v. Caldwell*, 5 Wis. 2d 146, 92 N.W.2d 356 (1958); *Fricke v. Fricke*, 257 Wis. 124, 42 N.W.2d 500 (1950). The basic rationale of these cases seems to have been that such agreements contributed to separation or divorce or represented an intrusion on the state's interest in seeing that divorced spouses are provided with sufficient support to avoid becoming wards of the state.

Commencing with the landmark decision in *Posner v. Posner*, 233 So. 2d 381 (Fla. 1970), *appeal after remand*, 257 So. 2d 530 (Fla. 1972), a more modern approach to the issue began to emerge through case law and legislation. This approach is to consider on a case-by-case basis the provisions in a marriage agreement relating to support, maintenance, and property settlement in the event of separation or divorce and to uphold them if the provisions are fair and reasonable. See *Dawley v. Dawley*, 551 P.2d 323 (Cal. 1976); *Volid v. Volid*, 286 N.E.2d 42 (Ill. App. Ct. 1972); *Freeman v. Freeman*, 565 P.2d 365 (Okla. 1977); *Unander v. Unander*, 506 P.2d 719 (Or. 1973).

Wisconsin adopted this approach by statute, accomplishing the change as part of the 1977 Divorce Reform Act, 1977 Wis. Laws ch. 105. Section 767.61(3)(L) (formerly section 767.255(3)(L) and 767.255(11)) states that any written agreement made by the spouses before or during marriage concerning any arrangement for property distribution will have a binding effect on the court in a divorce property division unless the agreement's terms are found to be inequitable as to either party. The court is to presume that an agreement is equitable as to both parties. The statute does not define *inequitable* or *equitable*.

In addition, section 767.56(8) states that agreements made before or during marriage concerning any arrangement for financial support are

entitled to consideration by the court in awarding maintenance to a spouse. In contrast to provisions relating to property division, provisions for financial support are not binding on the court.

Because the Wisconsin Marital Property Act did not change these provisions of chapter 767, both pre-Act marriage agreements (discussed generally in section 7.120, *supra*) and marital property agreements under the Act that purport to govern property divisions in the event of dissolution of the marriage will be reviewed for equitableness by the court at the time the marriage is terminated by divorce, legal separation, or annulment.

## **2. Test for Equitableness Under Button [§ 7.135]**

### **a. In General [§ 7.136]**

In *Button*, 131 Wis. 2d 84, the Wisconsin Supreme Court laid down specific standards for determining equitableness in pre-Act marriage agreements that are to be enforceable in the event of dissolution. The test established in *Button* does not relate precisely to either (1) the Wisconsin common-law standards adopted for pre-Act marriage agreements intended to be enforceable at death or (2) the statutory enforceability standards established for marital property agreements under the Act by section 766.58(6). Under *Button*, an agreement is inequitable under section 767.61(3)(L) (formerly subsections 767.255(3)(L) and (11)) if it fails to satisfy any one of the following three requirements:

1. Each spouse must make fair and reasonable disclosure to the other of his or her financial status.
2. Each spouse must enter into the agreement voluntarily and freely.
3. The substantive terms of the agreement dividing the property upon divorce must be fair to each spouse.

*Id.* at 89. The first two requirements, collectively referred to as *fairness in procurement*, are assessed at the time of the execution of the agreement. The third requirement, namely, the *substantive fairness* of the agreement, is assessed as of the execution of the agreement and, if

circumstances change significantly after execution of the agreement, also at the time of divorce. *Id.*

The court in *Button* began its discussion of the meaning of equitableness under the precursor to section 767.61(3)(L) by recognizing that the statute reflects two competing public-policy concerns. The first is freedom of contract. The legislature has recognized that premarital and postmarital agreements dividing property permit spouses or persons about to marry to “structure their financial affairs to suit their needs and values and to achieve certainty.” *Id.* at 94. The court pointed out that certainty encourages marriages and also is conducive to marital tranquility by protecting the parties’ financial expectations. The court then turned to the countervailing policy objective inherent in the statute: namely, the state’s interest in the legal status of marriage. A major component of that interest is the protection of both spouses’ financial interests in the event of dissolution. The circuit court in a divorce action must therefore carefully scrutinize an agreement between the spouses that deals with their financial affairs at dissolution.

### **b. Fairness in Procurement [§ 7.137]**

In connection with fairness in procurement, the court in *Button* stated that “[t]he public interest requires that a financial agreement between spouses or prospective spouses be executed under conditions of candor and fairness.” *Id.* at 95. Fair and reasonable disclosure of financial status is a significant aspect of this obligation and requires each party to disclose his or her assets, liabilities, and debts. The court specifically noted that independent knowledge of the other spouse’s financial status serves as a substitute for disclosure. *Id.*

In *Schumacher v. Schumacher*, 131 Wis. 2d 332, 388 N.W.2d 912 (1986), the Wisconsin Supreme Court applied the standards enunciated in *Button* to test the validity of a premarital agreement to control property division in a divorce action. The court held as a matter of law that the agreement was inequitable under section 767.255(11) (now section 767.61(3)(L)) because the parties did not fairly and reasonably disclose their assets to each other and did not have independent knowledge of each other’s financial status. It appeared that at the time of execution of their premarital agreement, the spouses did not exchange lists of their assets and liabilities, and that neither of them had a complete picture of the other’s financial condition. *Id.* at 340. In examining whether

sufficient independent knowledge existed to constitute a substitute for a fair and reasonable disclosure, the court observed that independent knowledge is not a general or imputed knowledge of the other party's assets and their value. At the same time, the requirement for fair and reasonable disclosure or independent knowledge is not so technical that de minimis failures to disclose will invalidate an agreement. *Id.* at 338. The court left open the question whether the parties to a pre-Act marriage agreement might waive disclosure without vitiating the agreement. *Id.*

Fairness in procurement also rests on a second key condition in addition to fair and reasonable disclosure, namely, that the agreement must be entered into voluntarily and freely. The relevant inquiry here is whether or not each spouse had “a meaningful choice.” The *Button* court cited four factors that a circuit court should consider in determining whether a party had a meaningful choice in executing a marriage agreement: “whether each party was represented by independent counsel, whether each party had adequate time to review the agreement, whether the parties understood the terms of the agreement and their effect, and whether the parties understood their financial rights in the absence of an agreement.” *Button*, 131 Wis. 2d at 95–96.

### **c. Substantive Fairness [§ 7.138]**

The *Button* court noted that the requirement of substantive fairness is an amorphous concept and one that must be determined on a case-by-case basis. The supreme court directed circuit courts to be mindful of the two principal legislative concerns reflected in the precursor to section 767.61(3)(L), namely, the parties' freedom to contract and the state's interest in protecting the parties' financial interests at dissolution. The court specifically noted that to meet the requirement of substantive fairness, the property arrangements in an agreement need not be equal between the parties or approximate the property division a circuit court might make under section 767.61 because to establish such a test would destroy the parties' meaningful right to contract. On the other hand, the agreement should “in some manner appropriate to circumstances of the parties take into account that each spouse contributes to the prosperity of the marriage by his or her efforts.” *Id.* at 96–97.

The court then discussed the then existing and reasonably foreseeable circumstances that the parties should consider in framing the agreement:

The parties should consider that the duration of the marriage is unknown and that they wish the agreement to govern their financial arrangements whether the marriage lasts a short time or for many years. The parties should consider such factors as the objectives of the parties in executing an agreement, the economic circumstances of the parties, the property brought to the marriage by each party, each spouse's family relationships and obligations to persons other than to the spouse, the earning capacity of each person, the anticipated contribution by one party to the education, training or increased earning power of the other, the future needs of the respective spouses, the age and physical and emotional health of the parties, and the expected contribution of each party to the marriage, giving appropriate economic value to each party's contribution in homemaking and child care services.

*Id.* at 97. The court did not discuss what would constitute adequate proof that the spouses had reflected on these matters in framing an agreement, thus emphasizing the importance of including appropriate factual recitations in the agreement's text.

The court concluded that a circuit court should look at the question of substantive fairness at the time the agreement was made to give effect to the parties' freedom to contract, noting that the parties at that time know their property and other relevant circumstances, are able to make reasonable predictions about the future, and should be able to draft a fair agreement if they take all the enumerated factors into account. *Id.* at 97–98. However, the court imposed a very significant qualification on the substantive fairness requirement. If there are significantly changed circumstances after the execution of an agreement that were not reasonably foreseeable when it was drafted, the circuit court should assess substantive fairness at the time of divorce as well as at the time of execution. This is done to determine whether, as a result of the significantly changed circumstances, “the agreement as applied at divorce no longer comports with the reasonable expectations of the parties.” *Id.* at 98–99.

➤ **Note.** Significantly changed circumstances may also be an element of the common-law defense of impracticability of performance, discussed in section 7.60, *supra*. This common-law defense appears to be available when enforcement of a marital property agreement is sought under section 766.58(6).

Finally, the court in *Button* noted that a determination of inequitableness under section 767.255(11) (now section 767.61(3)(L)) requires the circuit court to exercise its discretion:

A discretionary determination must be made on the basis of the facts and the applicable law. A discretionary determination must be the product of a rational mental process by which the facts of record and the law relied upon are stated and considered together for the purpose of achieving a reasoned and reasonable determination.

*Id.* at 99.

### **3. Tension Between Enforceability Standards Under Chapters 766 and 767 [§ 7.139]**

The Wisconsin Supreme Court's opinion in *Button* did not acknowledge the existence of the statutory standard for enforceability of marital property agreements in chapter 766, although the test for equitableness that it devised contains several of the same elements. Section 766.58(6) requires that the agreement be voluntarily entered into, that it be conscionable when made, and that it be accompanied by either fair and reasonable disclosure under the circumstances or notice of the other spouse's financial circumstances. The major difference between the two standards is the presence of the "significantly changed circumstances" qualification in the test for substantive fairness under the *Button* court's interpretation of the statute now found at section 767.61(3)(L). This qualification is not part of the statutory requirements for enforceability under section 766.58(6) and leads to tension between the two statutes. However, the failure to adopt this amendment may be viewed as expressing the legislature's intent not to disturb the equitable powers of the divorce court as much as its intent to apply differing standards for enforceability at death and at divorce. Clearly, the Wisconsin Supreme Court may construe "equitableness" for purposes of section 767.61(3)(L) to embody the precise elements of the statutory test for enforceability of marital property agreements in section 766.58(6) if it determines that this would be appropriate.

The "significantly changed circumstances" qualification seems unnecessary in applying section 766.61(3)(L) to marital property agreements entered into pursuant to the Act. If enforcement of a property-division provision in a marital property agreement that is valid

and enforceable when made would leave a spouse in a needy condition, the circuit court clearly has the power to avoid injustice by awarding maintenance. *See* Wis. Stat. § 767.56. This is true despite any provision in the agreement to the contrary, since such provisions are merely entitled to consideration by the court. *See* Wis. Stat. § 767.56(8).

There is some support for the proposition that the legislature intended that a different standard for enforceability of marital property agreements prevail at dissolution of the marriage than prevails during the marriage or at death. During the debate and floor action in the Assembly on Senate Substitute Amendment 1 to the 1983 Assembly Bill 200 (the bill that became 1983 Wisconsin Act 186), an amendment was offered that would have changed the language of section 767.255(11) (now section 767.61(3)(L)) to provide that a valid marital property agreement under chapter 766 was unconditionally binding on the divorce court, whereas other written agreements concerning any arrangements for property distribution were binding on the court only if the agreement's terms were equitable as to both parties. This amendment, Assembly Amendment 6 to Senate Substitute Amendment 1 to 1983 Assembly Bill 200, was tabled by the Assembly by a vote of 53 to 44, after the Assembly refused to reject it.

#### **4. Post-Button Decisions on Enforceability of Pre-Act Marriage Agreements at Dissolution [§ 7.140]**

In the wake of *Button*, the Wisconsin courts have had occasion to consider the reasonable foreseeability of a subsequent significant change in circumstances as they consider the enforcement of marriage agreements at divorce. In *Warren v. Warren*, 147 Wis.2d 704, 433 N.W.2d 295 (Ct. App. 1988), the Wisconsin Court of Appeals applied the principles enunciated in *Button* to uphold a premarital agreement when it was shown that an event not specifically covered by the agreement's terms, namely, the early retirement of one of the spouses, had been discussed during the negotiations. With reference to the foreseeability test, the court stated

The idea behind the test is that both spouses have a right to rely upon the prenuptial agreement when all subsequent events transpire as logically anticipated.

The premarital agreement is, after all, a contract with all of its attendant risks and risk bearing. Risk may be defined as uncertainty in regard to cost, loss, or damage. A. Kronman & R. Posner, *The Economics of Contract Law* 26 (1979). A person signing a premarital agreement undertakes all the normal anticipated risks that the agreement may not prove to be a wise one. Only when a future event can be said to have been too uncertain can it be said that the risk assumed is out of proportion to the loss incurred.

*Id.* at 710–11. Because the parties to the agreement in *Warren* not only foresaw the eventuality that one of the parties would take early retirement but also discussed it when the agreement was being negotiated, the spouse's early retirement was not viewed as an unforeseen changed circumstance that would justify disregarding the agreement.

The Wisconsin Court of Appeals has also been faced with the question whether the virtual abandonment of a postmarital agreement by the spouses constituted a significantly changed circumstance that warranted disregarding the agreement at divorce. In *Brandt v. Brandt*, 145 Wis. 2d 394, 427 N.W.2d 126 (Ct. App. 1988), the court answered in the affirmative, holding that the parties' disregard of a postmarital agreement would render its enforcement unfair at the parties' divorce. The agreement, entered into shortly after the spouses' marriage in 1952, provided that each spouse would maintain his or her separate estate. The agreement appears to have been executed to preserve the wife's expected inheritance from her family. The parties never discussed the marriage agreement during their estate planning or investment planning activities over the years, and the wife never attempted to maintain her inherited assets in such a way that they could be sufficiently identified and valued. On the contrary, the parties extensively commingled their assets over a long period to such an extent that it was impossible to trace the inherited property. The *Brandt* case establishes an important proposition with regard to the enforcement of marriage agreements at the time of dissolution: if the parties effectively disregard and abandon an agreement by their conduct, the abandonment will be viewed by the court as tantamount to a written waiver or revocation. *See also Krejci v. Krejci*, 2003 WI App 160, 266 Wis. 2d 284, 667 N.W.2d 780 (holding, on similar facts, that because of commingling of assets and consequent disregard of a premarital agreement it would be inequitable to enforce agreement at divorce).



In *Greenwald v. Greenwald*, 154 Wis. 2d 767, 454 N.W.2d 34 (Ct. App. 1990), both the procedural and the substantive fairness of a premarital agreement were challenged. *Greenwald* stands for the propositions that (1) a party's actual knowledge of the other party's financial condition is a satisfactory substitute for the procedural requirement of fair and reasonable disclosure of financial status, and (2) by itself, the fact of the parties' unequal bargaining position does not affect either the procedural requirement of voluntariness or the substantive requirement that the agreement be fair at the time of its execution. In addition, the *Greenwald* court held that the absence of separate counsel did not vitiate the spouses' premarital agreement.

Issues of procedural and substantive fairness in a premarital agreement were raised again in *Gardner v. Gardner*, 190 Wis. 2d 216, 527 N.W.2d 701 (Ct. App. 1994). The wife in a divorce action contended that the premarital agreement was procedurally unfair because the husband had failed to fairly disclose the actual value of his major asset, stock in a closely held business. She also contended that she had had "no choice" but to sign the agreement when the final version was presented to her three days before the wedding. The court concluded that the requirements of procedural fairness had been met. The husband had disclosed the value of his closely held stock, noting that (1) it was valued at book value and (2) its market value might be substantially higher. The wife's attorney, who had a background in accounting, had explained the difference between the two values to the wife but had made a professional judgment not to seek an independent appraisal. (He also advised the wife that the agreement overall was not in her best interest and that she should not sign it.) With respect to the timing of the agreement, discussions about it had begun in June 1985, and the wife and her attorney had received a draft in early August 1985. The wife had successfully negotiated changes in the agreement, to the extent of doubling her payout in the event of divorce. The court held that the husband's insistence that the agreement be signed before the couple's wedding in October 1985 was not coercive, in view of the fact that the wife was free not to proceed with the wedding if she found the agreement objectionable. The wife also attacked the substantive fairness of the agreement, arguing that the husband was awarded a disproportionate amount of property under the agreement's terms. It was clear from their financial disclosures at the time when the agreement was being negotiated that the husband had substantially greater assets than the wife. Citing *Greenwald*, 154 Wis. 2d at 787, the court pointed out that a premarital agreement is not unfair at divorce merely because the

application of the agreement results in a property division that is not equal between the parties. *Gardner*, 190 Wis. 2d at 234–35.

In a Wisconsin Supreme Court case involving a pre-Act marriage agreement, *Levy v. Levy*, 130 Wis. 2d 523, 388 N.W.2d 170 (1986), the court held that if the agreement by its terms applied only at termination of the marriage by the death of one of the spouses and was silent on the subject of property division or maintenance in the event of divorce, the agreement could not be relied on by the circuit court in arriving at a property division upon dissolution under section 767.255(11) (now section 767.61(3)(L)). It appears that the agreement in *Levy* was entered into before the 1977 Divorce Reform Act, at a time when the law did not permit contractual provisions for property division at divorce. In reaching its decision, the court accepted the view that a failure to specifically mention divorce in the agreement is fatal to acceptance of the agreement as binding for property-division purposes.

A nearly opposite result was reached in *Webb v. Webb*, 148 Wis. 2d 455, 434 N.W.2d 856 (Ct. App. 1988). In that case, the parties entered into a premarital agreement in October 1977 and subsequently married. The agreement recited that the parties desired to provide for their own children and/or grandchildren without regard to spouses' property rights as determined by Wisconsin law. The recitals couched the waiver of property rights not only in terms of each party's status as a surviving spouse, but also as husband and wife, respectively. In addition to this general language, the agreement specifically waived claims and rights in the other's estate that either party might acquire at death by reason of the contemplated marriage.

Although the agreement did not specifically state that it was to apply in the event of divorce, its language was drafted broadly enough to support that conclusion. The court was able to distinguish this case from *Levy* because there was evidence in the record that the parties intended the agreement to apply in the event of divorce. The drafter of the agreement testified that it was intended to apply both at death and at divorce. The *Levy* and *Webb* decisions illustrate the advisability of stating whether a marriage agreement either is or is not to apply to a property division in the event of dissolution.

## **F. Effectiveness of Pre-Act Marriage Agreements in Modifying Property Rights Arising Under the Act [§ 7.141]**

The saving provisions of section 766.58(12) regarding pre-Act marriage agreements are discussed in section 7.121, *supra*. The extent to which specific language used in pre-Act marriage agreements suffices to prevent the accrual of marital property after the determination date remains to be seen, assuming, of course, that the agreements are otherwise valid and enforceable under pre-Act law.

For example, the following questions are all likely to be raised in any construction of a pre-Act marriage agreement:

1. Is the agreement sufficient to bar the marital property interest that automatically arises under section 766.31(4) in the income from property titled in the name of one of the spouses or in the earned income of a spouse or in life insurance contracts and deferred employment benefits under the special rules in sections 766.61 and .62?
2. Does the agreement prevent deferred marital property elective rights under section 861.02 from being exercised with respect to property owned at death by a deceased spouse when it can be demonstrated that the property was acquired during the marriage and before the determination date and would have been marital property if the Act had been in effect?
3. Does the agreement avoid the operation of the mixed-property reclassification rule in section 766.63(1) if marital property assets become commingled with predetermination date property titled in the name of one of the spouses?
4. Does the agreement prevent the workings of the labor-appreciation rule in section 766.63(2) concerning increases in the value of a spouse's nonmarital property that result from his or her substantial undercompensated efforts?
5. Is mutual relinquishment of community property rights in general sufficient to reclassify or bar any or all of the above?

A number of these issues were presented in *In re Estate of Schaum*, No. 93-2858, 1995 WL 78251 (Wis. Ct. App. Feb. 28, 1995) (unpublished opinion not citable per section 809.23(3)). This case involved a pre-Act postmarital agreement in which the wife waived “all of her marital property rights” pursuant to former section 861.07(1) (1981–82) in return for certain testamentary provisions for her benefit upon the husband’s death. The issue before the court was whether this waiver was sufficient to bar the wife’s later claim to marital property and elective rights under the Act following the husband’s death in 1988. In an earlier appeal in the same case, *In re Estate of Schaum*, No. 91-0600 (Wis. Ct. App. Sept. 27, 1991) (unpublished opinion not citable per section 809.23(3)), the court held that the wife’s waiver of rights under former section 861.07(1) (1981–82) extended to the deferred marital property and augmented marital property estate elections under former sections 861.02 and 861.03, respectively, even though those elections were not in existence when the agreement was signed. The *Schaum* decisions are interesting, given the fact that the postmarital agreement was entered into in 1981 and waived rights under a statute (Wis. Stat. § 861.07(1) (1981–82)) that was repealed by the Act, effective January 1, 1986. The agreement used the term “marital property rights” without referring to rights arising under marital property legislation then under consideration in Wisconsin or under a system of community property ownership. Although the decisions contain no penetrating analysis and were not published, they represent at least one instance in which a Wisconsin appellate court was willing to construe a broad waiver of property rights in a pre-Act marriage agreement to reach both the accrual of marital property under the Act and the deferred marital property election created by it.

As the courts consider the construction of pre-Act marriage agreements in the future, it is desirable that a commonsense approach prevail. Many of these agreements were prepared to create separate property marriages at a time when there was no inkling that Wisconsin would one day adopt a system of community property. Even in agreements referring to relinquishment of community property rights, the language was often inadequate. Ownership under the Act (or under a community property system, for that matter) may exist apart from title. Therefore, references to relinquishment of rights by one spouse in property “owned” by the other must be read to refer to property “titled in” or “held by” the other to discover the desired intent. The spouses’ intent either to own their property as if they had never married or to relinquish all rights in the other’s property that accrue by virtue of

marriage permeates most pre-Act marriage agreements. Accordingly, the courts should honor that intent despite weaknesses in the phraseology actually used.

Consider some illustrative cases:

➤ *Example 1.* The spouses have a marriage agreement stating simply that they mutually relinquish their respective rights to an elective share and allowances under chapter 861 and that at death the property of each of them shall be subject to disposition free from any claim of the other. Assume that the spouses married in 1980 and that at the time of their marriage the wife has assets valued at \$200,000. These have increased in value to \$400,000 by January 1, 1986, and are valued at \$800,000 when the wife dies in 2006. The wife's will leaves \$100,000 to her husband and the balance to her children by a prior marriage. Further assume that most of the post-1985 increase in the value of the wife's assets results from uncompensated efforts and that mixing with nonmarital assets has occurred to the extent that tracing is difficult or impossible.

A significant question is whether the agreement nullifies the new property law classifications that commenced on January 1, 1986, or even the accrual of community property generally. Under the Act, marital property ownership interests may be accumulating from day to day in the assets held by each of the spouses. Although it is evident that the wife's intent is to leave only \$100,000 of her estate to her husband and the balance (\$700,000) to her children, that plan may be significantly disrupted if the husband petitions the probate court under section 857.01 for an order determining that up to one-half the assets titled in his wife's name represent his interest in marital property—a result that clearly might follow if the agreement is construed not to bar the accrual of marital property rights.

Despite these apparent problems, the agreement is still entitled to be construed in accordance with the parties' overall intent. When that intent is not clearly reflected in the agreement's language, it may be determined by resort to extrinsic evidence.

Before the death of either spouse, it would have been preferable to amend or redraft the agreement in Example 1 to clarify its effect. (Note that amendment may be difficult or impossible if one spouse is incompetent or unwilling to execute an amendment.) If the parties'

intent was to maintain their property in a manner consistent with the pre-Act common law rules of ownership so that the property titled in each spouse's name would pass in accordance with his or her existing will, then the parties should have taken appropriate steps to modify the agreement to negate the accrual of marital property. *See infra* § 7.154 (sample agreement).

Although the agreement in Example 1 may bar the deferred marital property election in section 861.02, it is less certain that the agreement will bar all spousal allowances granted under chapter 861, particularly the special allowance for support of a spouse under section 861.35.

➤ **Example 2.** The spouses have a marriage agreement stating that neither of them shall have or acquire any right, title, or interest in the other's real or personal property, and that each of them shall own all real and personal property that he or she now owns, or hereafter acquires, in his or her sole name, free from all rights or claims of the other, including any or all homestead, curtesy, dower, or elective rights in lieu thereof; spousal allowances; rights in intestacy; community property rights; or other statutory or common law rights, inchoate or otherwise. The agreement provides that each party shall have the absolute right during his or her lifetime to manage, control, dispose of, and otherwise deal with property in his or her name, now owned or hereafter acquired, without the other party's consent.

This agreement should be sufficient to avoid the accrual of marital property because it contemplates that property in either spouse's sole name, whenever acquired, is free of any "community property rights." Virtually all the key features of marital property contained in the Act and UMPA are derived from the laws of one or more of the eight community property states, and the legislature itself has declared in section 766.001(2) that marital property is a form of community property. Thus, the rule contained in section 766.31(4) classifying income on a spouse's property as marital property is analogous to similar rules of law in Louisiana, Texas, and Idaho; the concept of deferred marital property elections at death contained in sections 851.055 and 861.02 derives from former or current statutes in California and Idaho; the presumptions on mixed property are common to virtually all community property states; and so forth. *See supra* chs. 2, 3. By referring to ownership of property then owned or thereafter acquired in their sole names free of community property rights, the parties have evinced an intention to live separate in property. This intention should be respected by the courts, whether in

Wisconsin or some other community property jurisdiction. The specific language of section 766.58(12)(b) purports to make enforceable “a provision . . . intended to negate . . . any right . . . acquired under . . . a community property system.” If otherwise enforceable, the agreement should be construed to include marital property rights within the generic description of community property to prevent the accrual of marital property interests in either spouse’s assets or income. Accordingly, the agreement in Example 2 should not require revision.

➤ **Example 3.** The spouses have a marriage agreement providing that each party’s property interests, whether now owned or hereafter acquired, shall remain his or her separate and solely owned property, subject to his or her individual management and control, as if each were unmarried. Each party agrees that if he or she is the survivor, he or she will make no claim as surviving spouse to any part of the other’s estate, expressly relinquishing all claims of inheritance, dower, homestead, curtesy, or statutory right; spouse’s elective share; allowance; or privilege of a surviving spouse in or to the other’s property. The parties further agree that they will execute or join as a party in any deed or instrument that may be required by the other, or the other’s legal or personal representatives, for the purpose of divesting or preventing the accrual of any claims or rights waived and relinquished under the agreement.

This agreement evinces an intent to live separate in property, because it uses the words “as if each were unmarried.” It would be appropriate for the courts to effectuate that overall intent by holding that the agreement prevents the accrual of marital property interests in assets held in either spouse’s name. Even earned income can be considered handled indirectly by virtue of the spouses’ method of dealing with the assets into which it is converted. Here the reference to ownership, management, and control of property as if each spouse were unmarried should suffice to support such a construction.

Even if the language of Example 3 were viewed as inconclusive on the question of the spouses’ intent to give up community or marital property rights, the final sentence might provide a key to obtaining either a reformation of the agreement or a declaratory judgment to avoid the future accrual of marital property interests, if the parties could be shown to have intended to use pre-Act property rules in their marriage.

Without question, Example 3 presents a more difficult case than Example 2, because an intent to bar the accrual of marital property or community property must be inferred both from the document as a whole and from the specific reference to the relinquishment of all claims of “statutory right.” Although marital property rights under the Act are statutory in nature, the technical difficulty is that a spouse may not be making a *claim against* the other’s property in violation of the agreement even though *title* is held by the other. The marital property interests may be the spouse’s as a matter of right regardless of title. For example, the marital property interest in earned income and income generated by property arises at the same instant as the right to the income. This is not a *claim against* earnings and income that belong in their entirety to the other spouse, but rather a *property right in* the other spouse’s income that exists *ab initio*.

Another issue inherent in Example 3 is the effect of the language on postdeath allowances. Because allowances are specifically waived by the agreement, they should be barred to the extent that public policy permits.

Finally, Example 3 raises questions as to whether the agreement’s language absolves the spouses of the mutual obligation of support under sections 765.001(2) and 49.90(1m), assuming that the agreement in the example is otherwise silent on the subject of support. Because section 948.22(2) makes it a felony for any person intentionally to fail to provide spousal support that the person knows or reasonably should know he or she is obligated to provide, it is unlikely that the agreement could, as a matter of public policy, be construed to avoid spousal responsibilities of mutual support.

➤ **Example 4.** The marriage agreement contains provisions similar to those in Example 2 or Example 3, except that it also has the following language:

The parties have entered into this agreement in specific contemplation of the fact that Wisconsin has considered and may adopt a property law system based on community property. The parties intend and agree that such a law will have no effect with respect to their property, and that the property that they own or acquire and that would be classified as solely owned property under present Wisconsin law will continue to be treated in the same fashion. The parties further agree that their respective earned income, ordinary income from their separate investments, and increases



in the value of their separate property, however caused, will continue to be treated as separate property, and that neither of them shall assert any community property rights or quasi-community property elective rights to the other's assets or income.

The language in the agreement in Example 4 is clearly intended to take the spouses out of the Act. The courts should construe the agreement in a manner that accomplishes that intent, assuming that the agreement is otherwise enforceable. *See* Wis. Stat. § 766.58(12)(b); *see also supra* § 7.121.

➤ **Example 5.** The marriage agreement contains provisions similar to those in Example 3 and, in addition, obligates the spouse with the significantly larger estate to make a specific financial provision for the less-propertied spouse by will or revocable trust. Years after the Act's effective date, property that would be classified as marital property and as individual property under the provisions of the Act has become commingled with the spouses' predetermination date property in such a manner that the assets are essentially untraceable. The spouse with the larger estate then dies, leaving a will or revocable trust containing the required provision for the other spouse.

If the agreement's language were not interpreted to effectuate the spouses' apparent intent to live separate in property, this situation could produce a result of considerable unfairness. The less-propertied spouse might be entitled to one half of the spouses' entire combined estate because the commingled and untraceable assets are entirely reclassified as marital property by section 766.63(1). In addition, the less-propertied spouse would receive the specific financial provision that the deceased spouse was required to provide by will or revocable trust. The nonspousal beneficiaries of the decedent's estate might receive little or nothing. It is possible that the surviving spouse would be put to an equitable election under these circumstances. *See infra* ch.12.

## **G. Planning Considerations with Respect to Pre-Act Marriage Agreements [§ 7.142]**

### **1. In General [§ 7.143]**

The procedural and substantive requirements for marriage agreements intended to be enforceable at death or at dissolution under pre-Act law

have been discussed in sections 7.122–.140, *supra*. (For a discussion of the categories and attributes of pre-Act marriage agreements, see section 7.120, *supra*.) To recapitulate, a valid pre-Act marriage agreement must meet all the following requirements:

1. It must be in writing and signed by the party sought to be bound.
2. It must either make reasonable provision for a party who is giving up substantial rights or involve full and fair disclosure by both parties.
3. It must provide sufficient consideration to support the agreement. This requirement will usually be satisfied if one of the alternative conditions in item 2, above, is met.
4. It must be free from any taint of overreaching or fraud.
5. It must be equitable as to both parties, if it is to be enforceable as a property settlement agreement in the event of the dissolution of the parties' marriage.

The section 766.58(12) saving provisions for pre-Act marriage agreements, discussed at section 7.121, *supra*, provide that chapter 766 does not affect an otherwise enforceable document signed before the determination date unless the spouses provide otherwise in a marital property agreement made after the determination date. This section also confirms that provisions in such a document intended to negate, apply, or modify rights or obligations arising under the Act are enforceable after the determination date. Thus, provisions either to prospectively adopt or to prospectively abrogate marital property rights under the Act should be effective.

## **2. Marriage Agreements to Continue Common Law System of Property Ownership [§ 7.144]**

Before their determination date, spouses may wish to execute an agreement to prospectively abrogate marital property rights under the Act and to continue a common law system of property ownership. The advantages and disadvantages of doing so are discussed in detail in sections 7.110–.112, *supra*.

The courts have imposed no legal impediment to contractually altering or releasing future spousal property rights—at least with respect to those arising under the pre-Act property law system. See, for example, *Beat*, 25 Wis. 2d 315, and *Nickolay*, 249 Wis. 571, both of which involved the spouses' mutual surrender of possible future rights to make elections against one another's estates. In view of the specific statutory authorization of section 766.58(12)(b), there is no policy reason why contractual modification or negation of future spousal property rights under the property law system created by the Act should not also be fully recognized, at least so long as the rights of existing creditors, future creditors without notice, or other third parties acting in reliance on the status quo remain unaffected. This is supported by the Act's recognition of maximum contractual freedom to vary the Act's effect. See Wis. Stat. §§ 766.17, .58; UMPA § 3 cmt. (discussed in section 7.6, *supra*).

➤ **Example.** Assume that before the effective date of the Act, a married couple domiciled in Wisconsin enters into a marriage agreement to perpetuate the common law system of property ownership after their determination date (i.e., January 1, 1986). A primary reason they desire an agreement of this sort is so that their current estate plan can continue to be effective without significant modification after the determination date. In effect, they desire to nullify the Act's application to them. Their agreement is drafted to maintain the common law system of property ownership once the Act becomes effective, and they mutually relinquish any deferred marital property elective rights they may have or acquire. Further assume that the husband generates all the earned income in the family and holds title to most, if not all, of the significant investment assets. The wife has few assets in her sole name and no significant expectancies. They waive disclosure of their assets and net worth in the agreement. Because one of the agreement's primary purposes is to preserve the existing estate plan without the need for significant alterations, they intend to make no additional changes in their estate planning documents (i.e., wills and revocable trusts).

Assuming execution before 1986, the validity of the agreement will be judged under pre-Act law. (Even if the agreement were executed after April 4, 1984, the Act's standards for enforceability probably could not be met because of the wife's waiver of disclosure and assumed lack of actual knowledge.) Thus, a significant factor in the example is the wife's waiver of disclosure coupled with the possible lack of a reasonable

provision for, or consideration flowing to, her. In the absence of the agreement, after the determination date the wife would have a 50% ownership interest in the husband's earned income, the income from nonmarital property investments (in the absence of a unilateral statement), and the marital property portion of life insurance and deferred employment benefits. She would also have elective deferred marital property rights in certain property owned by the husband at the time of death, namely, property that was acquired during marriage, before the determination date, and that would have been marital property if the Act had been in effect throughout the marriage.

These are very substantial rights. Yet the agreement recited in the example makes no provision for the spouse in recognition that these property interests are given up. Moreover, because of the repeal of the spousal-elective-share provisions under prior law and the relinquishment of elective deferred marital property rights in the agreement, the wife would have virtually no protection if the husband subsequently decided to eliminate her entirely from his estate plan (although the contract might be unenforceable in the absence of some reasonable provision for the wife). The absence of any binding and adequate provision for the wife would make the agreement suspect under pre-Act law. *See supra* §§ 7.126, .127.

A fairly simple device might have been employed to salvage the agreement in the example. Assuming that the husband was unwilling to make disclosure but that the provisions for the wife in the husband's estate plan were reasonable in amount and nature, the husband and the wife might have agreed contractually that he was to maintain for her substantially equivalent provisions to those in his preexisting (or contemporaneously executed) will, revocable trust, or both. Their agreement might also have stipulated that he would not revoke, modify, or reduce those provisions without her consent. Alternatively, and again assuming the husband was unwilling to fully disclose, he might have agreed to make some reasonable specific financial provision for the wife at his death. In either case, it would have been desirable to include provisions for the wife, accompanied by the husband's agreement that he would not unreasonably deplete his probate or nonprobate estate through gifts or otherwise in such a manner as to make him unable to perform his obligations to the wife.

The agreement thus would become one providing for the wife by will or revocable trust. If the provision were adequate, the contract would be

valid and enforceable consideration for the wife's relinquishment of future marital property rights. *See Sipple v. Zimmerman*, 39 Wis. 2d 481, 493–94, 159 N.W.2d 706 (1968) (indicating that promise to make testamentary disposition in exchange for promise to make lifetime disposition may be enforced if consideration for mutual promises is adequate).

The facts in the example raise another question: if the agreement preserves the common law system of solely owned property for this marriage, makes no financial provision for the wife, and does not specifically waive the spouses' rights to elect against each other's wills, would the spousal-elective-share provisions contained in sections 861.03–.13 (1983–84) survive and be applicable? There is no definitive answer to this question, but if the spouses' intent to maintain the pre-Act property law system were sufficiently clear from the agreement, a court might find the elective share provisions applicable to avoid an inequitable result. Or the spouses might simply have agreed that the former statutory spousal elections would be available to the wife if the husband failed to make certain agreed-upon financial provisions for her.

Still another question is whether a marriage agreement executed before the determination date and designed to preserve the common law system of ownership can render inapplicable those statutory provisions that cannot be modified by a marital property agreement executed after the Act becomes effective. In particular, can the spouses choose not to be governed by section 766.15 (good faith duty between spouses), section 766.55(4m) (nonbinding effect of marital property agreement on creditors without actual knowledge), section 766.57(3) (nonbinding effect of marital property agreement on bona fide purchaser from spouse having management and control rights), section 859.18(6) (nonbinding effect of marital property agreement on property available for satisfaction of obligations at death of spouse), and section 766.58(2) (right of child to support)? If the pre-Act marriage agreement expressly refers to those statutory provisions, it is at least arguable that the savings provisions of section 766.58(12), *see supra* § 7.121, would allow the nullification of the statutory provisions. However, because many of the statutory provisions described above either are rooted in fundamental concepts of fairness or are designed to prevent fraud, the Wisconsin Supreme Court may, as a matter of public policy, adopt similar rules as a matter of common law if confronted with the appropriate case arising under pre-Act law.

### **3. Marriage Agreements to Classify All or Most Assets as Marital Property [§ 7.145]**

Some married couples may desire to enter into marriage agreements, before their determination date, to prospectively classify all their property as marital property. Some of the benefits and drawbacks of such classification are discussed in section 7.114, *supra*.

Just as spouses can make the Act prospectively inapplicable to them, they can also provide that all or most of their assets will be classified as marital property, and that other features of the Act will apply to their marriage, when the Act becomes effective as to them. *See* Wis. Stat. §§ 766.58(12)(b), .585. There are two ways to accomplish this objective. The first is for the spouses to enter into an anticipatory marital property agreement of the sort authorized by section 766.585(1). By law, no part of an anticipatory marital property agreement can apply before the determination date, and its enforceability is determined using the standards of section 766.58. *See supra* § 7.26. The second method is to insert provisions prospectively classifying property as marital property in a pre-Act marriage agreement, portions of which are intended to apply before the determination date. By virtue of section 766.585(3), an agreement of this sort is governed not by section 766.585 but rather by the saving provisions of section 766.58(12). *See supra* § 7.121. Those provisions require that the agreement be enforceable under the standards of law applicable when the agreement was executed.

The agreement should not be permitted to affect adversely the rights of creditors or third persons who have relied to their detriment on the continuation of the law applicable at the time of execution and the existing manner in which the spouses own their property. *See, e.g.*, Wis. Stat. § 766.55(2)(c), (4m).

### **4. Limited Marriage Agreements with Respect to Specific Assets or Liabilities [§§ 7.146]**

The Wisconsin cases involving pre-Act marriage agreements have invariably dealt with sweeping releases of property rights at death by one and sometimes both spouses. As a result, virtually no precedent exists regarding what is likely to become an increasingly important form of marriage agreement under the Act—the limited agreement.

It can be argued that the full requirements for a valid and enforceable pre-Act marriage agreement should not be applied to a limited marriage agreement. If the assets, liabilities, or issues are not substantial in relation to the spouses' overall economic situation and no significant property rights are surrendered, it can be maintained (assuming there is no full disclosure) that the reasonable-provision test for marriage agreements generally should not apply. It is also questionable whether full disclosure should be required for pre-Act limited marriage agreements; rather, the parties should be permitted to make mutual waivers of disclosure. Additionally, in dealing with limited marriage agreements, the parties' mutual promises and intent in entering into the agreement should be sufficient consideration to support it. Absent a showing of misrepresentation, undue influence, duress, or fraud, the limited marriage agreement should be recognized as valid.

Liberalizing the legal requirements for pre-Act limited marriage agreements tends to advance the strong public policy favoring agreements between spouses, *see supra* § 7.123, and in no way deprives the courts of the ability to protect the weaker spouse's interests when large economic issues are at stake. On the contrary, if the asset or liability that is the subject of the limited marriage agreement is a substantial element in the spouses' overall economic picture, the reasonable provision/full disclosure and adequate consideration requirements of pre-Act law will probably be applied to the agreement. *See supra* §§ 7.126, .127.

One situation in which pre-Act limited marriage agreements can play an important role is when one or both spouses have created an irrevocable life insurance trust to which employment-related or other life insurance policies have been assigned. In such cases, a limited marriage agreement executed before the Act's effective date, reclassifying the nongrantor spouse's interest in property used to pay premiums on the policies (or in the ownership interest or proceeds of the policies themselves), might avoid a number of difficult property classification and tax questions that could otherwise arise under the Act. *See infra* ch. 10.

## **H. Marriage Agreements Executed by Nonresidents Before Their Determination Date [§ 7.147]**

As time passes, fewer and fewer pre-Act Wisconsin marriage agreements are likely to come before the courts for interpretation. By the same token, the proportion of marriage agreements executed by nonresidents who subsequently move to Wisconsin is likely to increase. Thus, although the examples and discussion in sections 7.141 and 7.144–.146, *supra*, are couched in terms of spouses domiciled in Wisconsin before January 1, 1986, they apply equally to nonresident spouses who execute a marriage agreement either before or after January 1, 1986, and subsequently establish their domicile here. The major difference, of course, is that the applicable law for purposes of determining the enforceability of the agreement will be that of the jurisdiction where the spouses are domiciled when they execute the agreement. *See* Wis. Stat. § 766.58(12); *see also supra* § 7.121, *infra* ch. 13.

In addition, nonresident spouses intending to move to Wisconsin may wish to consider executing a statutory terminable individual property classification agreement (STIPCA) without disclosure as a temporary expedient to preserve their existing property arrangements for a three-year period. *See* Wis. Stat. § 766.589. The use of the STIPCA for this purpose is covered in section 7.74, *supra*.



## V. Sample Agreements [§ 7.148]

### A. Sample Agreement to Classify All or Most Property as Marital Property, with Option to Dispose of Spouses' Property at Death [§ 7.149]

#### 1. Introduction [§ 7.150]

The primary purpose of this agreement is to classify all or most of the spouses' property as marital property. It also contains an optional provision disposing of all of the spouses' property at death to a revocable trust jointly created by them. The agreement has been drafted for persons who are married to each other. If the form is to be used by parties who intend to marry, it may be modified accordingly. By its terms, the form is not intended to govern the division of the spouses' assets in the event of the dissolution of their marriage, although such provisions might be added if the parties desire. It is a sample form only and does not purport to be all-inclusive. Marital property agreements must be tailored to the parties' circumstances, and tax issues must be carefully considered. For other resources concerning the drafting of provisions for marital property agreements, see section 7.109, *supra*.

➤ **Note.** With respect to the methods by which spouses may classify or reclassify property, see section 766.31(10) and chapter 2, *supra*. See chapters 9 and 10, *infra*, for tax and estate planning considerations, respectively.

➤ **Caution.** Be careful in using this agreement if either or both of the spouses are not citizens of the United States. If the reclassification of property pursuant to the agreement results in a gift to the spouse who is not a United States citizen, there may be an immediate federal gift tax liability not sheltered by the marital deduction. See *infra* § 9.100.

## 2. Form [§ 7.151]

### MARITAL PROPERTY AGREEMENT

This is a marital property agreement between \_\_\_\_\_ and \_\_\_\_\_, husband and wife, of \_\_\_\_\_ County, Wisconsin.

WHEREAS, each party has made and acknowledges receiving a fair and reasonable disclosure under the circumstances of the parties' property and financial obligations,<sup>1</sup> as set forth in a separate Memorandum of Assets, Liabilities and Income executed by them on this date];

WHEREAS, the parties desire to classify property that they now own or hereafter acquire pursuant to Wisconsin law;

NOW, THEREFORE, it is agreed as follows:

#### I. ALL PROPERTY IS MARITAL PROPERTY

Except as otherwise provided in Article II, the parties agree that all assets of either or both of them, whether now owned or later acquired, shall be classified as marital property.<sup>2</sup> In determining whether an asset

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<sup>1</sup> There are no court decisions under the Act as to what constitutes a "fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations" for purposes of enforceability under section 766.58(6)(c). Inferentially, the financial disclosure statements that are included as part of the statutory terminable marital property classification agreement and the statutory terminable individual property classification agreement, *see infra* §§ 7.175, .178, should be sufficient. The memoranda of assets, liabilities, and income at sections 7.169 and .172, *infra*, should also be sufficient because they provide even greater detail than the statutory financial disclosure forms.

<sup>2</sup> By virtue of the definition of marital property in Article [XIII][XIV], Article I adopts all of Wisconsin's marital property rules, including the following:

a. The special terminable interest rules that apply to the marital property interest of a nonemployee spouse in a deferred-employment-benefit plan (including assets in a rollover IRA account traceable to such a plan), and to the marital property interest of a noninjured spouse in a recovery for loss of future income arising from a personal injury. Wis. Stat. §§ 766.62, .31(3), .31(7)(f).

b. The special classification rules for determining the marital property portion of life insurance policies and proceeds and the marital property portion of deferred employment benefits. Wis. Stat. §§ 766.61, .62.

is or is not classified as marital property for purposes of this agreement, the following rules shall apply:

#### **A. Special Rules with Respect to Assets Titled in Both Names**

1. Assets presently held jointly in the names of both parties with right of survivorship shall be classified as [marital property and shall be survivorship marital property unless the document of title, account under section 705.01(1) of the Wisconsin Statutes, brokerage account, registration of an uncertificated security, or partnership agreement is changed to indicate that the asset is no longer held with right of survivorship.] [marital property without right of survivorship.]<sup>3</sup> In

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c. The limitation on the marital property interest of a deceased spouse's estate in a life insurance policy owned by and insuring the surviving spouse. Wis. Stat. § 766.61.

d. The survivorship marital property rule with respect to homestead realty acquired in both spouses' names after the determination date. Wis. Stat. § 766.605.

To be clear about the applicability of the special rules listed above, an agreement to classify all or most property as marital property should specifically deal with these special rules by making them expressly applicable or inapplicable. The subsequent portions of Article I of the agreement deal with these issues. It is suggested that the drafter review with the client the effect the agreement will have on the following types of property:

- a. Tangibles;
- b. Gifts, inheritances, and interests in trusts created by third parties;
- c. Life insurance (including policies owned by one spouse and insuring the other's life and policies insuring third parties and used to fund cross-purchase agreements);
- d. Life insurance trusts;
- e. Stock in professional corporations;
- f. Deferred employment benefits (both qualified and nonqualified), including deferred compensation;
- g. IRAs;
- h. Assets subject to a specific bequest to a child or other third parties;
- i. Real estate or tangible personal property located in other jurisdictions;
- j. Assets that have substantially declined in value; and
- k. Recoveries for personal injury.

The optional provisions in the balance of Article I of the agreement are designed to present alternative methods of dealing with some of these assets. It is suggested the drafter consider whether new documents of title (e.g., deeds, stock certificates, etc.) should be prepared to inform third parties of ownership changes made by the agreement.

<sup>3</sup> A marital property agreement provision may be ineffective to negate the survivorship feature of a joint bank account under chapter 705, particularly in

addition, the parties confirm that any previously acquired homestead that is survivorship marital property (or other assets held in the names of both parties as survivorship marital property) shall remain survivorship marital property.

2. Assets acquired in the future in the names of both parties shall be classified as marital property without right of survivorship unless the document of title, account under section 705.01(1) of the Wisconsin Statutes, brokerage account, registration of an uncertificated security, or partnership agreement clearly states that there is a survivorship feature, in which case the asset shall be survivorship marital property. [A homestead acquired in the future exclusively in the names of both parties shall be survivorship marital property unless the document of title specifies otherwise.]<sup>4</sup>

### **B. Deferred Employment Benefits**

1. This agreement does not purport to classify deferred employment benefits while held by a qualified plan under ERISA for the benefit of a party who is a participant in the plan.<sup>5</sup> When the benefits are distributed to, or withdrawn from a qualified plan by the party who is the plan participant, such benefits [shall be classified as the individual property of the party who was the plan participant] [shall be classified as marital property].

2. Deferred employment benefits held in a deferred employmentbenefit plan that is not a qualified plan under ERISA [shall be classified as the individual property of the party who is the plan participant] [shall be classified as marital property].

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the case of account agreements executed before the marital property agreement was entered into. The same may be true of survivorship provisions in a joint brokerage account agreement. *See supra* § 7.118. To the extent that it is important to achieving the purposes of their marital property agreement, or would create undesirable results under their combined estate plan, the spouses should close out such accounts and reopen them as marital property accounts or tenancy-in-common accounts without a right of survivorship.

<sup>4</sup> Delete the bracketed phrase if the statutory rule of section 766.605 is not desired.

<sup>5</sup> This provision acknowledges the preemption by federal law governing ERISA-qualified deferred-employment-benefit plans of any contrary provisions of state community property laws. *See Boggs v. Boggs*, 520 U.S. 833 (1997). The benefits are what they are under federal law as long as they remain in the plan. Once the benefits are distributed or withdrawn from the plan, however, the agreement purports to classify them.

3. Any marital property interest of the nonemployee party in a deferred-employment-benefit plan (or rollover IRA account) terminates as provided by sections 766.31(3) and 766.62(5) of the Wisconsin Statutes if the nonemployee party predeceases the employee party.<sup>6</sup>

4. The interest of a party in an individual retirement account or similar arrangement (IRA), including an IRA created by rollover of deferred employment benefits previously held by a qualified plan, shall be classified in the same manner as withdrawn or distributed deferred employment benefits in this agreement. For this purpose, the party holding the IRA shall be considered the employee/plan participant, and the IRA shall be considered a benefit provided as a result of employment.

[5. The special time-based apportionment rules in section 766.62 of the Wisconsin Statutes [shall not be applied for the purpose of determining the marital property interest of each party in deferred employment benefits; rather, each party shall own a present undivided one-half interest as marital property in such benefits] [shall be applied for the purpose of determining the marital property interest of each party in deferred employment benefits].]<sup>7</sup>

### **C. Life Insurance Policies and Proceeds**

1. The special time-based apportionment and other ownership rules in section 766.61 of the Wisconsin Statutes [shall not be applied for the purpose of determining the marital property interest of each party in the ownership interest and proceeds of life insurance policies on each of their lives. Rather, each party shall own an undivided one-half interest as marital property in the ownership interest and proceeds of each such policy [, except that a life insurance policy owned by one party on the life of the other is the individual property of the party who is owner regardless of the classification of property used to pay premiums on the policy]]<sup>8</sup> [shall be applied for the purpose of determining the marital

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<sup>6</sup> This treatment not only is consistent with Wisconsin statutory law, but also appears to be in accord with *Boggs v. Boggs*, 520 U.S. 833 (1997), with respect to benefits held by a qualified plan under ERISA.

<sup>7</sup> This paragraph should be used only if deferred employment benefits (including IRA accounts) are classified as marital property under this paragraph. The second option in the sentence (i.e., preserving the time-based apportionment rules found in the statute) is not recommended because of its complexity.

<sup>8</sup> The alternative choices in the first sentence permit the drafter either to select a simple rule that grants each spouse an equal one-half ownership interest in each policy and its proceeds or to adopt the classification and ownership rules with respect to life insurance found in section 766.61(3), including the time-

property interest of each party in the ownership interest and proceeds of life insurance policies on each of their lives].<sup>9</sup>

2. The marital property interest of a deceased party's estate in an insurance policy designating the surviving spouse as the owner and insured [shall] [shall not] be subject to the limitations of section 766.61(7) of the Wisconsin Statutes.<sup>10</sup>

#### **D. Personal Injury Recovery for Loss of Future Income**

*[Choose appropriate alternative]*<sup>11</sup>

The marital property interest of the noninjured party in a personal injury recovery of damages for loss of future income terminates if the noninjured party predeceases the injured party.

*[Or]*

The marital property interest of the noninjured party in a personal injury recovery of damages for loss of future income does not terminate if the noninjured party predeceases the injured party but remains owned by

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based apportionment rules. If the parties wish to adopt the simple classification rule but continue the rule of section 766.61(3)(c) that a life insurance policy owned by one spouse on the other spouse's life is the owner's individual property, the final clause of the first bracketed choice should be used. Special provisions should be made for life insurance policies required to be maintained by a spouse pursuant to a decree dissolving a prior marriage, *see* Wis. Stat. § 766.61(5), and for policies required to be maintained pursuant to a cross-purchase agreement for a business interest.

<sup>9</sup> *See supra* note 7.

<sup>10</sup> The alternative choices in this sentence permit the drafter either to adopt or to negate the frozen interest rule in section 766.61(7). If the insured spouse survives, that rule limits the property rights of the deceased noninsured spouse's estate to one half the marital property interest in the interpolated terminal reserve and unearned premium at the time of death.

<sup>11</sup> The first alternative preserves the special statutory rule in sections 861.01(3m) and 766.31(7m) that treats a personal injury recovery of damages for loss of future income as terminable interest marital property if the noninjured spouse dies first; the second alternative negates the statutory rule, thus making this portion of a recovery of damages "pure" marital property. The second alternative permits the property interest of a predeceasing noninjured spouse in the recovery to be disposed of at death to persons other than the surviving injured spouse.

the noninjured party and may be disposed of upon the death of the noninjured party regardless of the order of the parties' deaths.

*[Continue]*

## **II. INDIVIDUAL PROPERTY**

**A.** The following assets shall be classified as individual property:

1. Assets acquired by either or both of the parties [in the future] through gift, inheritance, or distributions from trusts established by a third party.<sup>12</sup>

2. Currently owned beneficial interests in irrevocable trusts established by the other party or by third parties.

3. The personal effects, consisting of jewelry, clothing, and items of personal adornment, presently held by each party. To the extent consistent with the parties' obligations to act in good faith toward one another, personal effects acquired after the date of this agreement shall be the holding party's individual property, regardless of the classification of property used to make the acquisition.

[4. Each party shall own as his or her individual property each life insurance policy insuring his or her life regardless of the classification of any property used to make premium payments or additions. This classification shall extend to any and all replacement policies or supplemental life insurance or accidental death and disability contracts issued in connection with any such policy. Any property transferred to an irrevocable trust holding a life insurance policy insuring the life of either party shall, at the time of such transfer, be classified as the individual property of the party whose life is insured by the policy, including any premium or additions paid pursuant to a split-dollar agreement or with regard to group or other insurance paid by the employer of a party. The party designated as the owner of a life insurance policy insuring the life of a third party shall own such policy as his or her individual property regardless of the classification of property used to make premium payments or additions.]<sup>13</sup>

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<sup>12</sup> If either of the spouses has received or anticipates receiving significant gifts or inheritances, excluding these from the operation of the agreement may be desirable.

<sup>13</sup> Paragraph C of Article I should be deleted if this subparagraph is used. The drafter should be aware that this provision may raise ethical considerations in a dual-representation situation if the assets classified as individual property

**B.** The classification of an asset as individual property shall extend to the realized or unrealized appreciation in the value of such asset regardless of whether the appreciation occurred through general market conditions or through the application of labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity by either or both of the parties; and to property received in exchange for or with the proceeds of the asset. [The classification of an asset held by one or both of the parties shall not be affected by the classification of property added to or mixed with the asset, and any addition or mixing shall be deemed a gift to the holding party or parties.]<sup>14</sup> [By signing this agreement, each party is exercising his or her unilateral right under section 766.59 of the Wisconsin Statutes to classify income on individual property as individual property.]<sup>15</sup>

### **III. RECLASSIFICATION OF PROPERTY**

Nothing in this agreement shall prevent the parties from reclassifying marital property assets as the individual property assets of one party by gift, marital property agreement, [unilateral statement,] consent, or otherwise as permitted by law.

### **IV. MANAGEMENT AND CONTROL**

*[Insert any special provisions regarding management and control of marital property assets here. In the absence of such provisions, the management and control features of Wisconsin's marital property laws control.]*

### **V. AGREEMENT NOT TO AFFECT PROPERTY DIVISION IN EVENT OF DISSOLUTION**

In the event of the dissolution of the parties' marriage by divorce, annulment, legal separation, or other legal proceeding, this agreement

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are substantial because the agreement adopts a classification rule contrary to that in the Act. *See infra* ch. 14.

<sup>14</sup> Caution should be exercised in using the bracketed provision. Depending on the nature of the assets classified as individual property, this provision may permit one spouse unilaterally to convert marital property into the individual property of that spouse.

<sup>15</sup> Note that Paragraph B of Article II does not automatically classify the *income* on property received by gift, inheritance, etc., as individual property. Such income will be marital property unless the drafter adds the bracketed final sentence, which treats the agreement as a signing party's unilateral statement pursuant to section 766.59 with respect to such property.



shall not affect how the court divides the parties' assets pursuant to section 767.255 of the Wisconsin Statutes or the comparable statute of any applicable jurisdiction.<sup>16</sup> Except as otherwise necessary to enforce provisions intended to survive dissolution, this agreement is revoked by and shall terminate upon entry of a court judgment of dissolution of the parties' marriage.

*[Add Article VI if appropriate]*

## VI. DISPOSITION AT DEATH

The parties on this date created and anticipate that they will continue to have a joint revocable trust known as the \_\_\_\_\_ and \_\_\_\_\_ Revocable Trust of 20\_\_\_. If, at the death of the first of the parties to die, the deceased party's will (whether or not it is probated) gives the residue of his or her estate to the revocable trust, then the interest of [the deceased party] [both parties] in assets classified as marital property and in assets other than marital property shall immediately pass without probate to the trustee of the revocable trust, except that any interest in the tangible personal property of the deceased party shall directly pass without probate to the surviving party. In addition, at the death of the first of the parties to die, some or all of the marital property assets may be divided on the basis of aggregate value rather than item by item. The surviving spouse and the successor in interest to the deceased party's share of marital property may enter into an agreement providing how some or all of the marital property assets in which each has an interest will be divided based on aggregate value. If, at the death of the second of the parties to die, that party's will (whether or not it is probated) gives the residue of his or her estate to the revocable trust, then the assets of that spouse (including all after-acquired property) shall pass without probate to the revocable trust, provided that the second party to die may at any time amend this agreement with respect to the property to be disposed of at his or her death. This article is intended to be a

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<sup>16</sup> CAUTION: Although the agreement does not purport to govern how the court divides the spouses' assets in the event of dissolution of the marriage, it may be relevant to the *characterization* of those assets for purposes of division. See *Bonnell v. Bonnell*, 117 Wis. 2d 241, 344, N.W.2d 123 (1984). Thus, if property acquired by gift or inheritance is classified as marital property by the agreement, the property may be subject to division in the event of dissolution. In addition, future changes in statutory or case law may cause the property classifications accomplished in the agreement to have a substantive impact at dissolution despite any language in the agreement to the contrary. Specific language should be included if the agreement is to function as a settlement agreement in the event of divorce, separation, or annulment.

disposition of property as described in section 766.58(3)(f) of the Wisconsin Statutes.<sup>17</sup>

*[Continue]*

#### **[VI.][VII.] FINANCIAL DISCLOSURE**

Each party has made [a written] disclosure to the other of his or her property and obligations in connection with the preparation and execution of this agreement. Each party acknowledges receiving such disclosure from the other and represents that his or her own disclosure was fair and reasonable under the circumstances.

#### **[VII.][VIII.] AMENDMENT OR REVOCATION**

This agreement may be amended or revoked only by a later written marital property agreement.

#### **[VIII.][IX.] BINDING EFFECT**

This agreement shall be binding on the parties and their heirs, legatees, personal representatives, and legal representatives.

#### **[IX.][X.] GOVERNING LAW**

This agreement shall be interpreted in accordance with the laws of the state of Wisconsin, where the parties now reside and are domiciled.

#### **[X.][XI.] CHANGE OF DOMICILE**

This agreement determines the classification of assets owned or acquired while both parties are domiciled in Wisconsin, including assets traceable thereto following a change in domicile to another state. The classification of other assets acquired after either or both are domiciled in

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<sup>17</sup> Article VI should be used only if the parties have a joint revocable trust and intend to use the agreement as a will substitute agreement to fund the joint revocable trust. A simpler version of a will substitute agreement is found at section 7.163, *infra*. If the parties intend to use the agreement as a will substitute agreement and each has a revocable trust, this provision may be modified so that each spouse's share of marital property, plus his or her other property, passes at death to his or her own revocable trust.

another state shall be determined by the laws of the domiciliary state and not by this agreement.<sup>18</sup>

#### **[XI.][XII.] SEVERABILITY**

All provisions contained in this agreement are severable. If a provision is held to be invalid by any court, this agreement shall be interpreted as if the invalid provision were not contained herein.<sup>19</sup>

#### **[XII.][XIII.] REVOCATION OF PRIOR AGREEMENTS**

By execution of this agreement, the parties hereby revoke each and every marriage agreement previously entered into by them, including each and every marital property agreement pursuant to Wisconsin's marital property laws. The parties further agree that any such agreement shall be of no further force and effect in any respect, as if it had never been entered into.<sup>20</sup>

#### **[XIII.][XIV.] DEFINITIONS**

Except as otherwise provided in this agreement, the terms *held*, *individual property*, *marital property*, and *deferred employment benefit* shall be interpreted in accordance with and shall have the incidents provided under Wisconsin law [as amended to date].<sup>21</sup> An "asset" or "assets" shall consist of property rights and interests of any nature or description, whether present or future, legal or equitable, vested or contingent, in real or personal property, and shall include assets that either or both of the parties have transferred to a revocable trust of which either or both are the settlor(s).

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<sup>18</sup> The treatment of Wisconsin marital property removed to another jurisdiction upon the change of domicile of one or both spouses is discussed in chapter 13, *infra*.

<sup>19</sup> If the invalidity of one provision would make the enforcement of the remainder of the agreement inappropriate, modification of this provision should be considered. *See supra* § 7.70.

<sup>20</sup> Note that if certain actions taken or certain property classifications established by earlier agreements are to be preserved, special provisions should be included for that purpose.

<sup>21</sup> See note 4, *supra*, for a discussion of the scope of the marital property definition. Use the bracketed language at the end of the sentence if the definitions are to be restricted to the law in effect at the time the agreement is executed. If the definitions are to "float" with the evolution of Wisconsin law following the date of execution of the agreement, the bracketed language should be deleted.

**[XIV.][XV.] LEGAL REPRESENTATION**

[Before signing this agreement, each party consulted with an attorney of his or her choice.]<sup>22</sup> [The parties are represented by one attorney in connection with this agreement, and each has agreed in writing to such dual representation.]<sup>23</sup> Each party has received from his or her attorney an explanation of the terms and legal significance of this agreement. Each party acknowledges that he or she understands this agreement and its legal effect and is signing voluntarily.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
(party's signature)

\_\_\_\_\_  
(party's signature)

STATE OF WISCONSIN  
COUNTY OF \_\_\_\_\_

This instrument was acknowledged before me on \_\_\_\_ (date) \_\_\_\_ by  
\_\_\_\_ (name) \_\_\_\_ and \_\_\_\_ (name) \_\_\_\_.

\_\_\_\_\_  
Notary Public, State of Wisconsin  
My commission expires \_\_\_\_\_

*[If a Memorandum of Assets, Liabilities, and Income is to be used, see §§ 7.169 and .172, infra.]*

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<sup>22</sup> See generally *infra* ch. 14 (separate representation).

<sup>23</sup> In the event of a conflict of interest, the consent to dual representation must be in writing after consultation. See SCR 20:1.7; see also ch. 14, *infra*.

## **B. Sample Agreement to Classify All or Most Property as Individual Property [§ 7.152]**

### **1. Introduction [§ 7.153]**

The primary purpose of this agreement is to classify all or most of the spouses' property as individual property. This agreement has been drafted for use either by persons who are married to each other or by persons contemplating marriage. It is a sample form only and does not purport to be all-inclusive. Marital property agreements must be tailored to the parties' circumstances, and tax issues must be carefully considered. For other resources concerning the drafting of provisions for marital property agreements, see sections 7.109, *supra*. With respect to the methods by which spouses may classify or reclassify property, see section 766.31(10) and chapter 2, *supra*. See chapters 9 and 10, *infra*, for tax and estate planning considerations, respectively.

### **2. Form [§ 7.154]**

#### **MARITAL PROPERTY AGREEMENT**

*[Choose appropriate alternative]*

This is a marital property agreement between \_\_\_\_\_ and \_\_\_\_\_, husband and wife, of \_\_\_\_\_ County, Wisconsin.

*[Or]*

This is a marital property agreement entered into in contemplation of marriage between \_\_\_\_\_, of \_\_\_\_\_ County, Wisconsin, and \_\_\_\_\_, of \_\_\_\_\_ County, Wisconsin.

WHEREAS, the parties intend to marry;

WHEREAS, \_\_\_\_\_ [and \_\_\_\_\_] [was] [were] previously married, and \_\_\_\_\_ [and \_\_\_\_\_] [has] [have] [a child] [children] from [his] [her] [their] previous marriage[s];<sup>1</sup>

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<sup>1</sup> Recitals explaining the spouses' circumstances and the reasons for the agreement may be inserted at this point.

[Continue]

WHEREAS, the parties desire by this agreement to determine the system of property classification and ownership applicable during their marriage and upon the termination of their marriage [by divorce, annulment, legal separation, or other legal proceeding, or] by the death of one or both of the parties, both as to assets that they now own and as to those they hereafter acquire;

WHEREAS, each party has made and acknowledges receiving a fair and reasonable disclosure under the circumstances of the parties' property and financial obligations<sup>2</sup> [, as set forth in a separate Memorandum of Assets, Liabilities, and Income executed by them on this date];

WHEREAS, each party understands that the income and assets of the other may increase in the future, such as by reason of inheritances, gifts, compensation, business profits, realized or unrealized appreciation, accumulated income, and other increases or additions, or may decrease, such as by reason of investment reverses, business losses, general market decline, illness or disability, loss of employment, or other cause, and each party acknowledges that he or she is entering into this agreement regardless of the level of present or future income of the other party or the present or future value of the other party's assets;

WHEREAS, each party understands that in the absence of this agreement the law would confer upon him or her property rights and interests in certain of the present and future assets possessed or acquired by the other, and each party further understands that those rights and interests will be affected by this agreement;

WHEREAS, the parties desire to classify, pursuant to Wisconsin law, all present and future assets of either or both of them as individual property and none as marital property except as otherwise specifically provided in this agreement;

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<sup>2</sup> There are no court decisions under the Act as to what constitutes a "fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations" for purposes of enforceability under section 766.58(6)(c). Inferentially, the financial disclosure statements that are included as part of the statutory terminable marital property classification agreement and the statutory terminable individual property classification agreement, *see infra* §§ 7.175, .178, should be sufficient. The memoranda of assets, liabilities, and income at sections 7.169 and .172, *infra*, should also be sufficient because they provide even greater detail than the statutory financial disclosure forms.

WHEREAS, the parties further desire to provide that all obligations now outstanding and hereafter incurred by either of them shall be their respective sole obligations, as if they were unmarried persons;

NOW, THEREFORE, it is agreed as follows:

## **I. ALL PROPERTY IS INDIVIDUAL PROPERTY**

**A.** The parties agree that all of the assets of either or both of them shall be classified as individual property and none of their assets shall be classified as marital property except as otherwise provided in this agreement.<sup>3</sup> In carrying out that intention, the following rules shall apply:

**1.** An asset now or hereafter held by a party shall be classified as that party's individual property.

**2.** Unless expressly provided to the contrary in a document of title or other writing signed by both parties, an asset now or hereafter held by both parties shall be classified as the individual property of both parties as joint tenants with right of survivorship.

**3.** An asset not held by a party shall be classified as the individual property of a party to the extent that such party (a) furnished the consideration in money or money's worth (including the incurring of a debt) for the asset; or (b) received the asset by gift, inheritance, nontestamentary transfer, or trust distribution. The parties recognize that assets acquired as described in (a) and (b) above may be co-owned as individual property. The parties further agree that when one party furnishes the consideration for an asset that he or she gives to the other party, the asset is the individual property of the donee party.

**B.** The classification of an asset as individual property shall extend to the income from the asset; to the realized or unrealized appreciation in the value of the asset regardless of whether such appreciation occurred through general market conditions or through the application of labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity by either or both of the parties; and to property received in exchange for or with the proceeds of the asset. The classification of an asset held by one or both of the parties shall not be affected by the classification of property added to or mixed with the asset, and any addition or mixing shall be deemed a gift to the holding party or parties.

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<sup>3</sup> If the parties wish to classify certain of their assets as marital property or to hold certain assets as survivorship marital property, a mechanism is provided in Article II of the agreement.

**C.** By way of illustration and not of limitation, the following assets shall be classified as individual property:

1. All compensation, earnings, and income generated by a party through the provision of services, labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity;

2. All deferred employment benefits attributable to the services of a party, including all pensions, retirement benefits, and deferred compensation;

3. All claims, causes of action, or recoveries of whatever nature for personal injury or property damage sustained by a party;

4. All life insurance policies and annuities, and all disability, health, and accident policies of which a party is designated as the owner on the records of the policy issuer or the employer;

5. All business and investment property of a party, including all bank accounts, stocks, bonds, notes, debentures, sole proprietorships, partnerships, limited liability companies, joint ventures, patents, copyrights, royalty interests, real estate, and individual retirement accounts (IRAs) or similar arrangements;

6. All distributions from partnerships, limited liability companies, corporations, and joint ventures, all income from sole proprietorships, rents, interest, dividends, royalties, and all other income received from the investments or assets owned by a party;

7. All beneficial interests of a party in an estate or in a trust created by either party or by a third person, including all distributions of principal or income from an estate or a trust;

8. All gifts to a party, whether from the other party or a third party;  
and

9. All undivided interests in property owned by a party as a joint tenant or tenant in common with the other party and/or with third parties.

## **II. MARITAL PROPERTY**

Notwithstanding any other provision in this agreement, an asset shall be marital property only if this classification either is expressly stated in the document of title to the property or, as to either held assets or assets that are not held, is expressly stated in a written instrument signed by



both parties. An asset classified as marital property can be held as survivorship marital property if the survivorship form of holding is expressly stated in the document of title to the property or other written instrument signed by both parties.

### III. SUPPORT AND OBLIGATIONS

*[Choose appropriate alternative]<sup>4</sup>*

*[Alternative I]*

*[Choose appropriate Paragraph A]*

**A.** Because \_\_\_\_\_ has and is likely to continue to have more individual property than \_\_\_\_\_, \_\_\_\_\_ agrees to assume primary responsibility for providing support for the parties in the form of food, clothing, shelter, transportation, insurance, health care, and other expenditures consistent with an appropriate standard of living for the parties. If either party files an action seeking dissolution of the marriage by divorce, annulment, legal separation, or other legal proceeding, this paragraph shall have no further effect.

*[Or]*

**A.** Each of the parties is financially able to provide for his or her own support at an appropriate standard of living, and the parties shall share approximately equally in the financial responsibility for providing support for the parties in the form of food, clothing, shelter, transportation, insurance, health care, and other expenditures consistent with an appropriate standard of living for the parties. If either party files an action seeking dissolution of the marriage by divorce, annulment, legal separation, or other legal proceeding, this paragraph shall have no further effect.

*[Or]*

**A.** Each of the parties is capable of contributing to their combined support. The parties shall agree from time to time during their marriage on the proportions and/or amount to be contributed by each, taking into account their then current employment status, health, and other relevant circumstances. The parties recognize and acknowledge that under this

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<sup>4</sup> The general purpose of the alternative paragraphs in Article III is to attempt to provide for the financial security of both parties. The alternatives are samples only and must be tailored to the parties' specific circumstances.

paragraph the primary responsibility for providing support may shift from one party to the other at various times during the course of their marriage. If either party files an action seeking dissolution of the marriage by divorce, annulment, legal separation, or other legal proceeding, this paragraph shall have no further effect.

[Or]

**A.** Each of the parties is financially able to provide for his or her own support at an appropriate standard of living, and each shall be financially responsible for himself or herself. Except as otherwise required by law, neither shall be responsible for providing support for the other in the form of food, clothing, shelter, transportation, insurance, health care, or other similar expenditures.

[Continue]

**B.** [The responsibility for self-support and all] [All] other obligations, including but not limited to contractual obligations and those for torts, punitive damages, penalties, fines, or forfeitures that either party has incurred or hereafter incurs, and the parties' respective shares of obligations that have been or may be incurred jointly, either with each other or with third persons, shall be the obligations of the incurring party as though he or she were an unmarried person, regardless of when the obligation is incurred. Unless prohibited by law, any such obligation shall be satisfied exclusively out of the individual property of the incurring party as defined by this agreement. If a creditor obtains payment or satisfaction in connection with the obligation of a party out of the individual property of the other party as defined by this agreement, the other party shall be entitled to full reimbursement from the incurring party or his or her estate.

**C.** Each party shall provide all prospective credit grantors (except those for normal support) with a copy of this agreement before the time credit is granted or an open-end credit plan is entered into.<sup>5</sup>

**D.** Either party may voluntarily pay or satisfy an individual obligation of the other in whole or in part. The payment or satisfaction shall not be deemed to be an assumption of the obligation by the contributing party

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<sup>5</sup> It is not yet entirely clear whether furnishing a copy of *excerpts* from the agreement will suffice to bind creditors under sections 766.55(4m) and 766.56(2)(c). If the parties are reluctant to disclose their entire marital property agreement to creditors, the provisions applicable to debt and credit could be included in a separate marital property agreement.

nor shall it be deemed to be a waiver of this article as to any other obligation.

*[Or]*

*[Alternative II]*

**A.** Except for obligations for normal support and maintenance, neither party shall incur without the other's written consent a contractual obligation that may be satisfied from the individual property of the other party as defined by this agreement. Each party shall provide a copy of this agreement to all credit grantors (except those for normal support and maintenance) before the time credit is granted or an open-end credit plan is entered into.<sup>6</sup>

**B.** If a creditor obtains payment or satisfaction in connection with a contractual or noncontractual obligation of a party out of the individual property of the other party as defined by this agreement, the other party shall be entitled to full reimbursement from the incurring party or his or her estate.

*[Continue]*

#### **IV. MANAGEMENT AND CONTROL**

**A.** Each party shall have full and exclusive power of management and control over his or her individual property free from any interference or claims of the other party. Each party shall have the unqualified right to dispose of his or her individual property at any time by sale, exchange, gift, will, beneficiary designation, trust arrangement, or otherwise to any person or persons he or she may choose without the other party's consent [except as provided in Article [VI][VII]].<sup>7</sup> If asked by the other party or by any grantee or donee of the other party, a party shall join in any deed, mortgage, or other conveyance of individual property necessary for the purpose of documenting that he or she has no right, claim, or interest in the property conveyed or for the purpose of perfecting a clear record title to the property [; however, the foregoing shall not apply to conveyances of homestead real estate]. The foregoing provisions shall constitute consent under section 767.215(2)(i) of the Wisconsin Statutes that each party may continue to unilaterally manage

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<sup>6</sup> *See id.*

<sup>7</sup> The bracketed language should be included if financial provisions for a spouse are made in Article [VI][VII].

and control his or her individual property after commencement of an action to dissolve the marriage.

**B.** If asked by the other party, a party shall execute any spousal waivers and consents or take any other action necessary under the provisions of the Employee Retirement Income Security Act of 1974, the Retirement Equity Act of 1984, or any similar laws, to relinquish any right, claim, or property interest arising out of such law in any employment benefits attributable to the other party's employment or self-employment and shall allow the other party to name any beneficiary and to elect any settlement option under any employment benefit plan.<sup>8</sup>

**C.** Either party may make provision for the other by gift, will, beneficiary designation, trust arrangement, or otherwise, and neither party shall be precluded by virtue of this agreement from receiving and enjoying the benefits of such provisions. The making of any such provision shall not constitute a waiver of any of the provisions of this agreement.

*[Add Article V if appropriate]*

## **V. PROPERTY AND SUPPORT RIGHTS UPON DISSOLUTION OF MARRIAGE**

### **A. Property Division**

*[Choose appropriate alternative]*

If there is a dissolution of the parties' marriage by divorce, annulment, legal separation, or other legal proceeding, each party shall have the absolute right to retain all his or her individual property, and that property shall not be subject to division pursuant to section 767.61 of the Wisconsin Statutes. Assets held by the parties as joint tenants with right of survivorship shall be divided equally between the parties, and assets held as tenants in common shall be divided between the parties according to their respective percentage ownership interests. If the parties acquire marital property or survivorship marital property pursuant to Article II, those assets shall be divided equally between the parties.

*[Or]*

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<sup>8</sup> Regarding the enforceability of this provision, see section 2.214, *supra*. See chapter 9, *infra*, for a discussion of possible gift tax issues.

If there is a dissolution of the parties' marriage by divorce, annulment, legal separation, or other legal proceeding, \_\_\_\_\_ agrees to transfer property to \_\_\_\_\_ as a full and final settlement of [his] [her] rights to a property division under section 767.61 of the Wisconsin Statutes, as follows:

*[Insert appropriate provisions. A phase-in of financial benefits, in trust or outright, may be appropriate. Several factors may be relevant, including the length of the marriage, the birth of children, the ages of children, the parties' health, the completion of education, the receipt of anticipated inheritances, and the like.]*

Subject to the foregoing, each party shall have the absolute right to retain all his or her individual property. Assets held by the parties as joint tenants with right of survivorship shall be divided equally between the parties, and assets held as tenants in common shall be divided between the parties according to their respective percentage ownership interests. If the parties acquire marital property or survivorship marital property pursuant to Article II, those assets shall be divided equally between the parties.

*[Continue]*

Each party agrees to pay all debts incurred by him or her, and all other liabilities or obligations imposed on him or her, and each agrees to hold the other harmless from all such debts, liabilities, or obligations. The parties agree to share equally all joint obligations. Each party agrees to pay his or her own attorney fees and disbursements in connection with the dissolution proceeding.

## **B. Maintenance**

If either party files an action seeking the dissolution of the marriage by divorce, annulment, legal separation, or other legal proceeding, the parties agree that no temporary alimony or maintenance payments shall be awarded to either party. If the action results in the termination of the parties' marriage or in a legal separation, both parties waive any entitlement to alimony or maintenance, and neither party shall be awarded any limited or permanent alimony or maintenance payments of any kind. Each party specifically acknowledges that by accepting the benefits of other provisions of this agreement, he or she is estopped from requesting or accepting maintenance.<sup>9</sup>

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<sup>9</sup> Section 767.56 provides that any mutual agreement of the parties on the issue of maintenance is only a factor to be considered by the divorce court, that

[Or]

In lieu of temporary maintenance, which is specifically waived by both parties, \_\_\_\_\_ agrees to pay \_\_\_\_\_ within 30 days of service of a petition for dissolution of the marriage the sum of \$\_\_\_\_\_ for each full year of marriage, with the duration of the marriage measured from the wedding date to the date that a petition for dissolution of the marriage is filed, but in no event less than \$\_\_\_\_\_ nor more than \$\_\_\_\_\_.

### **C. Stipulation**

If either party files an action seeking the dissolution of the marriage by divorce, annulment, legal separation or other legal proceeding, the parties agree to enter into a written stipulation carrying out the provisions of this article.

### **D. Miscellaneous**

The parties specifically affirm that this agreement is at this time a fair and equitable written agreement under section 767.61 of the Wisconsin Statutes relating to property division and a mutual agreement under section 767.56 of the Wisconsin Statutes relating to maintenance payments. If either party files an action seeking the dissolution of the marriage, the parties intend that this agreement shall be deemed equitable as to both of them at the time of its execution and at all times thereafter.<sup>10</sup> The parties realize that the value of the individual property owned by each of them and the earning capacity or experience of each of them may significantly increase or decrease in the future, and they acknowledge that any such increase or decrease shall not constitute a change of circumstances affecting the equitableness of this agreement.

[Continue]

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is, such agreements are not binding on the court. This provision is one possible approach, and may be used when the parties' property division is intended to cover their entire financial settlement. Under other circumstances, the provision of maintenance may be appropriate.

<sup>10</sup> To be enforceable upon dissolution under section 767.61(3)(L), a marital property agreement must be equitable as to both parties both at the time of execution and also when the parties' marriage is dissolved. *See Button v. Button*, 131 Wis. 2d 84, 388 N.W.2d 546 (1986). The tests for determining whether or not an agreement will be considered equitable are discussed in detail in sections 7.107 and .133–.140, *supra*. It is not certain to what extent the parties can agree that the agreement will be considered equitable in the future regardless of the circumstances.

#### **[V.][VI.] WAIVER OF PROPERTY RIGHTS UPON THE DEATH OF EITHER PARTY**

[Except as otherwise provided in Article [VI][VII], each] [Each] party waives and releases all rights, claims, and property interests, of whatever nature, under the present or future laws of Wisconsin or any other jurisdiction, that he or she might otherwise have or acquire as a result of the death of the other party in or to the individual property of the other party. This article is intended to apply to all rights and property interests acquired as a result of the parties' marriage including, but not limited to, [rights of intestate succession,]<sup>11</sup> dower and curtesy, rights to elect against the will, the deferred marital property elective share, community property, quasi-community property rights, marital property, and, to the extent permitted by law, spousal support allowances and rights of selection; provided, however, that this article shall not divest the surviving party of his or her one-half interest in marital property or of his or her interest in survivorship marital property to the extent that such marital or survivorship marital property was acquired pursuant to Article II. Neither party shall make or assert any claim or ownership right of any kind in or to the individual property of the other as a result of the death of the other, except:

1. Claims for satisfaction of a bona fide debt or to enforce a right under this agreement;

2. Rights to property given or devised to the party by will or transferred to the party by nontestamentary, nonprobate disposition; and

[3.Rights of intestate succession.]<sup>12</sup>

Each party shall join in the execution and filing of any instrument or conveyance and take any other action necessary to relinquish or otherwise avoid the effects of the law of any jurisdiction conferring any right or interest relinquished above; if the other party's legal representative or successor in interest so requests. [If either party leaves assets passing by the laws of intestate succession of any jurisdiction, those assets shall be distributed as if the surviving party had

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<sup>11</sup> Delete bracketed language if number 3 is left in.

<sup>12</sup> If the surviving spouse is *not* to receive the individual property described in the agreement in the event the owner dies intestate, number 3 should be deleted and the two bracketed sentences dealing with intestacy near the conclusion of Article [V][VI] should be left in. If the surviving spouse is to receive the individual property by intestate succession, leave in number 3 and strike the later bracketed sentences.

predeceased the deceased party. If necessary, the surviving party shall execute any instrument required to disclaim any assets that would otherwise pass to him or her under the laws of intestate succession.] [Neither party shall act as a personal representative of the other's estate unless nominated pursuant to the terms of the other's will.]

#### **[VI.][VII.] PROVISION FOR SPOUSE**

*[Insert agreed-upon reasonable provisions and/or possible gift restrictions for the benefit of the spouse giving up significant rights. Phased-in financial provisions based on the length of the marriage may be appropriate in some circumstances. Alternatively, the financial provisions might consist of a promise to transfer a specific amount of property at death or to maintain provisions for the spouse substantially identical to those in the current estate plan. This article might also provide that if the arrangement or plan for a spouse were not maintained, the survivor would have certain remedies and elective rights defined in the agreement. An example of an outright gift or gifts might be as follows:]*

**[A.** If     (husband)     dies while the parties are married to each other and     (wife)     survives him by 30 days,     (husband)     agrees to make the following provisions for     (wife)     in his will or other estate planning documents, and     (wife)     agrees to accept these provisions in lieu of any other provisions that might be available to her as the surviving spouse under applicable law:

1. If     (wife)     survives     (husband)     by 30 days,     (husband)     shall give to     (wife)     any interest he owns in their then principal residence[, free of any mortgages or liens,] and in the contents of the principal residence, including all household furniture, furnishings, goods, and effects intended for utilitarian or ornamental use.

2. If     (wife)     survives     (husband)     by 30 days,     (husband)     shall give to     (wife)     [property with a net after-tax value of \$ \_\_\_\_\_] [[an amount] [a fractional share of the residue of the estate] equal to \_\_\_\_\_% of the amount by which     (husband's)     gross estate as defined in section 2031 of the Internal Revenue Code (and any successor provisions thereto) as finally determined for federal estate tax purposes exceeds funeral expenses, administration expenses, debts, mortgages, and liens that are allowed as deductions in     (husband's)     estate for federal estate tax purposes].

**B.** If     (wife)     dies while the parties are married to each other and     (husband)     survives her by 30 days,     (wife)     agrees to make the



following provisions for (husband) in her will or other estate planning documents, and (husband) agrees to accept such provisions in lieu of any other provisions that might be applicable to him as the surviving spouse under any applicable law:

1. If (husband) survives (wife) by 30 days, (wife) shall give to (husband) any interest she owns in their then principal residence[, free of any mortgage or liens] and in the contents of the principal residence, including all household furniture, furnishings, goods, and effects intended for utilitarian or ornamental use.

2. If (husband) survives (wife) by 30 days, (wife) shall give to (husband) [property with a net after-tax value of \$\_\_\_\_\_] [[an amount] [a fractional share of the residue of the estate] equal to \_\_\_\_\_% of the amount by which (wife's) gross estate as defined in section 2031 of the Internal Revenue Code (and any successor provisions thereto) as finally determined for federal estate tax purposes exceeds funeral expenses, administration expenses, debts, mortgages, and liens that are allowed as deductions in (wife's) estate for federal estate tax purposes].]

#### **[VII.][VIII.] TAXES**

The parties shall file joint United States and state income tax returns for each calendar year for which a joint return will result in less aggregate United States and state income taxes than would result from their filing separate returns. The income tax liability due with respect to any such joint return shall be allocated between the parties and paid by each of them out of his or her respective individual property, and if either party is required to pay the tax obligation of the other, the party liable shall hold the other harmless for amounts paid on his or her behalf. The amount paid by each party shall bear the same ratio to the total tax payable with respect to the joint return as the amount of tax that would be payable by him or her if he or she filed a separate return bears to the total tax that would be payable by the parties if both filed separate returns<sup>13</sup> [; provided, however, that if one party would have paid less total tax by filing a separate return instead of a joint return with the tax allocations provided for by this article, that party shall pay the lesser amount and the other party shall pay the balance owed pursuant to the joint return]. If the parties file a combined state income tax return, then for purposes of determining how the combined income tax obligation shall be allocated

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<sup>13</sup> This method of apportionment generally follows that found in former Treas. Reg. § 1.6015(b)-1(b). A somewhat simpler method of apportionment is to allocate the taxes in proportion to the respective adjusted gross incomes of each of the spouses.

between them, the deductions and tax credits shall be attributed to each party in the same ratio as the state total income of each bears to the total state total income. Any additional assets, penalties, interest, or costs arising out of any audit or other adjustment shall be allocated between the parties as provided in this article. Each party may, but shall not be obligated to, join in any gifts made by the other for federal or state gift tax reporting purposes.

## **[VIII.][IX.] MISCELLANEOUS PROVISIONS**

*[Choose appropriate alternative]<sup>14</sup>*

### **A. Scope of Agreement**

This agreement governs the parties' property rights and obligations and the economic incidents of their marriage during the marriage and upon the death of either or both of them. In the event of the dissolution of the parties' marriage by divorce, annulment, legal separation, or other legal proceedings, this agreement shall not affect how the court divides the parties' assets, as provided in section 767.61 of the Wisconsin Statutes or the comparable statute of any applicable jurisdiction. Except as otherwise necessary to enforce provisions intended to survive a dissolution, this agreement is revoked by and shall terminate upon entry of a court judgment of dissolution of the parties' marriage.

*[Or]*

### **A. Scope of Agreement**

This agreement governs the parties' property rights and obligations and the economic incidents of their marriage during the marriage, upon the dissolution of the marriage by divorce, annulment, legal separation, or other legal proceeding, and upon the death of either or both of them. Except as otherwise necessary to enforce provisions intended to survive a dissolution, this agreement is revoked by and shall terminate upon entry of a court judgment of dissolution of the parties' marriage.

*[Continue]*

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<sup>14</sup> If optional Article V is used, *supra*, the first alternative should be deleted and the second alternative should be used.

## **B. Financial Disclosure**

Each party has made [a written] disclosure to the other in connection with the preparation and execution of this agreement of his or her property and obligations. Each party acknowledges receiving such disclosure from the other and represents that his or her own disclosure was fair and reasonable under the circumstances.

## **C. Entire Agreement**

This agreement represents the entire agreement and understanding between the parties regarding the property and obligations described herein. Both parties acknowledge that neither party has made any conflicting or additional promise or representation to the other regarding any of the subject matter covered by this agreement.

## **D. Amendment or Revocation**

This agreement shall not be amended or revoked except by a later marital property agreement.

## **E. Binding Effect**

This agreement shall be binding on the parties and their heirs, legatees, personal representatives, and legal representatives.

## **F. Governing Law**

This agreement shall be interpreted in accordance with the laws of the state of Wisconsin, where the parties now reside and are domiciled. The establishment by either or both of the parties of a residence or domicile in another state shall not affect the binding nature or validity of this agreement, the parties' rights under it, or the laws under which it shall be interpreted.

## **G. Change of Domicile**

If necessary to validate this agreement and make its substance enforceable in a jurisdiction in which the parties later become domiciled, the parties (or their legal representatives) agree to reexecute this agreement or one that is in substantially the same form and accomplishes the same objectives, all in accordance with the requirements of such jurisdiction.

## H. Severability

All provisions contained in this agreement are severable. If any of them shall be held to be invalid by any court, this agreement shall be interpreted as if such invalid provisions were not contained in the agreement.<sup>15</sup>

## I. Revocation of Prior Agreements

By execution of this agreement, the parties revoke each and every marriage agreement previously entered into by them, including each and every marital property agreement pursuant to Wisconsin's marital property laws. The parties further agree that any such agreement shall be of no further force and effect in any respect, as if it had never been entered into.<sup>16</sup>

## J. Definitions

Except as otherwise provided in this agreement, the terms *held*, *individual property*, *marital property*, and *deferred employment benefit* shall be interpreted in accordance with and shall have the incidents provided under the laws of Wisconsin [as amended to date].<sup>17</sup> For purposes of this agreement, *individual property* also includes individual property under the laws of any other jurisdiction adopting the Uniform Marital Property Act or some variant thereof, separate property under the laws of any community property jurisdiction, and common-law property interests under the laws of any common-law jurisdiction. *Marital property* also includes marital property under the laws of any other jurisdiction adopting the Uniform Marital Property Act or some variant thereof, and community property under the laws of any community property jurisdiction. An *asset* or *assets* shall consist of property rights and interests of any nature or description, whether present or future, legal or

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<sup>15</sup> If the invalidity of one provision would make the enforcement of the remainder of this agreement inappropriate, modification of this provision should be considered. *See supra* § 7.70.

<sup>16</sup> Note that if certain actions taken or certain property classifications established by earlier agreements are to be preserved, special provisions should be included for that purpose.

<sup>17</sup> See footnote 2 of the marital property agreement at section 7.151, *supra*, for a discussion of the scope of the marital property definition. Use the bracketed language at the end of the sentence if the definitions are to be restricted to the law in effect at the time the agreement is executed. If the definitions are to “float” with the evolution of Wisconsin law following the date of execution of the agreement, the bracketed language should be deleted.

equitable, vested or contingent, in real or personal property, and shall include assets that either or both of the parties have transferred to a revocable trust of which either or both are the settlor(s).

#### **K. Legal Representation**

[Before signing this agreement, each party consulted with an attorney of his or her choice.]<sup>18</sup> [The parties are represented by one attorney in connection with this agreement, and each has agreed in writing to such dual representation.]<sup>19</sup> Each party has received from his or her attorney an explanation of the terms and legal significance of this agreement. Each party acknowledges that he or she understands this agreement and its legal effect and is signing voluntarily.

#### **L. Effective Date**

[This agreement becomes effective upon the marriage of the parties.] [This agreement becomes effective upon the date that both parties are domiciled in Wisconsin.] [This agreement becomes effective upon the later of the marriage of the parties or the date that both parties are domiciled in Wisconsin.] [This agreement becomes effective upon execution.]

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<sup>18</sup> See generally *infra* ch. 14 (separate representation). If optional Article V (relating to property and support rights upon dissolution) is included, dual representation is inappropriate. See ch. 14, *infra*.

<sup>19</sup> In the event of a conflict of interest, the consent to dual representation must be in writing after consultation. See SCR 20:1.7; see also ch. 14, *infra*.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
(party's signature)

\_\_\_\_\_  
(party's signature)

STATE OF WISCONSIN  
COUNTY OF \_\_\_\_\_

This instrument was acknowledged before me on     (date)     by  
    (name)     and     (name)    .

\_\_\_\_\_  
Notary Public, State of Wisconsin  
My commission expires \_\_\_\_\_

*[If a Memorandum of Assets, Liabilities, and Income is to be used, see §§ 7.169 and .172, infra.]*

### CERTIFICATION

Each of the undersigned certifies that he or she is an attorney, duly licensed to practice law in the state of Wisconsin; that \_\_\_\_\_ has been employed by \_\_\_\_\_ and \_\_\_\_\_ has been employed by \_\_\_\_\_; that each has advised and consulted with his or her client with respect to the client's rights and has explained to the client the legal significance of the foregoing agreement and the effect that it has upon the client's rights otherwise conferred as a matter of law; that each party, after being advised by his or her respective counsel, acknowledged to the undersigned that he or she understood the agreement and that he or she has executed the agreement freely and voluntarily; and that each undersigned has no reason to believe that his or her client did not understand the agreement and that he or she did not freely and voluntarily execute this agreement [, such execution being in the presence of each of the undersigned].

Dated: \_\_\_\_\_.

\_\_\_\_\_,  
Attorney for

\_\_\_\_\_,  
Attorney for

**C. Sample Agreement for Classification of Certain Assets (Limited Marital Property Agreement)**  
**[§ 7.155]**

**1. Introduction [§ 7.156]**

The primary purpose of this agreement is to provide for (1) the classification of one or more assets or (2) specific rights and responsibilities (such as management and control) with regard to certain items of property. With respect to the treatment of liabilities, see the alternative versions of Article III of the agreement in section 7.154, *supra*, for examples. The agreement has been drafted for use either by persons who are married to each other or by persons contemplating marriage. It is a sample form only and by definition does not purport to be all-inclusive. Marital property agreements must be tailored to the parties' circumstances, and tax issues must be carefully considered. For other resources concerning the drafting of provisions for marital property agreements, see section 7.109, *supra*. With respect to the methods by which spouses may classify or reclassify property, see section 766.31(10) and chapter 2, *supra*. See chapters 9 and 10, *infra*, for tax and estate planning considerations, respectively.

**2. Form [§ 7.157]**

**MARITAL PROPERTY AGREEMENT**

*[Choose appropriate alternative]*

This is a marital property agreement between \_\_\_\_\_ and \_\_\_\_\_, husband and wife, of \_\_\_\_\_ County, Wisconsin.

*[Or]*

This is a marital property agreement entered into in contemplation of marriage between \_\_\_\_\_, of \_\_\_\_\_ County, Wisconsin, and \_\_\_\_\_, of \_\_\_\_\_ County, Wisconsin.

WHEREAS, the parties intend to marry;

WHEREAS, \_\_\_\_\_ [and \_\_\_\_\_] [was] [were]  
previously married, and \_\_\_\_\_ [and \_\_\_\_\_] [has] [have]  
[a child] [children] from [his] [her] [their] previous marriage[s];

*[Continue]*

WHEREAS, the parties desire to classify certain assets they now own  
or hereafter acquire pursuant to Wisconsin law;

*[Describe the purpose or purposes of the agreement. These might  
include one or more of the following:*

*1. Classifying certain assets held by each spouse or by both spouses,  
either as individual property or as marital property;*

*2. Classifying income on predetermination date property and/or  
individual property now owned or hereafter acquired as individual  
property;*

*3. Agreeing that the deferred marital property election in sections  
861.02 to 861.06 does not apply to some or all property owned by the  
spouses;*

*4. Providing specific management and control rights with respect to  
certain assets;*

*5. Classifying as individual property funds used to pay premiums on  
life insurance policies owned by the spouses, by third parties, or by  
irrevocable life insurance trusts; or, alternatively, relinquishing marital  
property rights in specific life insurance policies owned by the spouses or  
by third parties, even if marital property is used to pay premiums;*

*6. Agreeing that either spouse can designate the beneficiary of  
specific life insurance policies or specific deferred employment benefits  
without the other spouse's consent, and that the spouse with the power  
to designate the beneficiary can reclassify any marital property or  
deferred marital property rights to components in the policy as his or her  
individual property;*

*7. Granting general or limited unilateral authority to one or both  
spouses to make gifts of marital property and waiving any remedy with  
respect thereto or to bar gifts of marital property without joinder by both  
spouses; and*



8. *Fixing responsibility on one of the spouses for payment of certain obligations, including the granting of a right of reimbursement to the nonobligated spouse if marital property is used to pay the indebtedness.*

*Assuming that the agreement's purpose is to classify certain enumerated assets as individual property, the following recital might be included:]*

[WHEREAS, the parties desire to avail themselves of the right contained in section 766.58 of the Wisconsin Statutes to classify certain assets owned by or titled in the names of one or both of them as their respective individual property;]

WHEREAS, each party has made and acknowledges receiving a fair and reasonable disclosure under the circumstances of the parties' property and financial obligations<sup>1</sup> [, as set forth in a separate Memorandum of Assets, Liabilities, and Income executed by them on this date];<sup>2</sup>

WHEREAS, each party understands that in the absence of this agreement the law might confer on him or her property rights and interests in certain of the property that is classified as the individual property of the other in this agreement, and each party by this agreement relinquishes all such rights and property interests in such property;

NOW, THEREFORE, it is agreed as follows:

#### **I. HUSBAND'S INDIVIDUAL PROPERTY**

The parties agree that the following assets shall be classified as the individual property of \_\_\_\_\_:

*[Describe the assets]*

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<sup>1</sup> There are no court decisions under the Act as to what constitutes a "fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations" for purposes of enforceability under section 766.58(6)(c). Inferentially, the financial disclosure statements that are included as part of the statutory terminable marital property classification agreement and the statutory terminable individual property classification agreement, *see infra* sections 7.175, .178, should be sufficient. The memoranda of assets, liabilities, and income at sections 7.169 and .172, *infra*, should also be sufficient because they provide even greater detail than the statutory financial disclosure forms.

<sup>2</sup> Full and detailed disclosure of the sort involved in completing a memorandum of assets, liabilities, and income may not be necessary for a limited marital property agreement. *See supra* § 7.116.

## II. WIFE'S INDIVIDUAL PROPERTY

The parties agree that the following assets shall be classified as the individual property of \_\_\_\_\_:

*[Describe the assets]*

## III. INCOME; [ADDITIONS;] APPRECIATION; EXCHANGES

The classification of an asset as the individual property of a party shall extend to income from the asset; [to additions to the asset regardless of the classification of the funds or property used to make or acquire the addition;]<sup>3</sup> to realized or unrealized appreciation in the asset's value, regardless of whether that appreciation occurred through general market conditions or through the application of labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity to the asset by either of the parties without receiving reasonable compensation therefor; and to property received in exchange for or with the proceeds of the asset.<sup>4</sup>

## IV. MANAGEMENT AND CONTROL

During their marriage, each party shall have full and exclusive powers of management and control over those assets classified as his or her individual property under this agreement.

## V. RIGHT TO DISPOSE OF INDIVIDUAL PROPERTY

Each party shall have the absolute and unqualified right to dispose of assets classified as his or her individual property under this agreement, at any time, by sale, exchange, gift, disposition at death, or otherwise, to any person or persons he or she may choose, including the other party.

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<sup>3</sup> Caution should be exercised in using the bracketed provision. Depending on the nature of the assets classified as individual property, this provision may permit one spouse unilaterally to convert marital property into the individual property of that spouse.

<sup>4</sup> If an interest in a closely held business is included in the property classified as individual property, the parties may wish to modify the final phrase of this sentence so that it does *not* apply to publicly traded securities or cash received in exchange for the closely held-business interest.

## VI. RIGHT OF REIMBURSEMENT

If a creditor obtains satisfaction from assets that are classified under this agreement as the individual property of one of the parties, and the party owning the assets is not personally liable for the obligation, that party shall be entitled to reimbursement of such amount from the other party if the other party is personally liable for the obligation or from the estate of such party if the other party is deceased. The amount reimbursed shall be the individual property of the recovering party.

*[Add Article VII if appropriate]*

## VII. PROPERTY RIGHTS UPON DISSOLUTION OF MARRIAGE

If there is a dissolution of the parties' marriage by divorce, annulment, legal separation, or other legal proceeding, each party shall have the absolute right to retain all his or her individual property, and that property shall not be subject to division pursuant to section 767.61 of the Wisconsin Statutes nor shall the value of the individual property be considered in dividing the parties' other property interests. The parties specifically affirm that this agreement is at this time a fair and equitable written agreement under section 767.61 of the Wisconsin Statutes relating to property division. If either party files an action seeking dissolution of the marriage, the parties intend that this agreement shall be deemed equitable as to both of them at the time of its execution and at all times thereafter.<sup>5</sup>

*[Continue]*

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<sup>5</sup> The normal limited marital property agreement used for estate planning purposes would include neither optional Article VII nor optional Article [VII] [VIII]. Instead, the drafter would proceed directly to Article [VIII][XIX]. However, if the agreement is classifying assets that represent a significant portion of one or both spouses' estates, these optional provisions might be included. Note that unless the property classified as individual property by this agreement in fact was received by inheritance or gift, it may be subject to division by the court under section 767.61 in the event of dissolution. To avoid this result, the parties must specifically agree that the property is not subject to division and is to be awarded to the party who is designated the owner. To be enforceable upon dissolution under section 767.61(3)(L), a marital property agreement must be equitable as to both parties both at the time of execution and also when the parties' marriage is dissolved. See *Button v. Button*, 131 Wis. 2d 84, 388 N.W.2d 546 (1986). The tests for determining whether or not an agreement will be considered equitable are discussed in detail in sections 7.107 and .133–.140, *supra*.

*[Add Article [VII][VIII] if appropriate]*

**[VII.][VIII.] WAIVER OF PROPERTY RIGHTS UPON DEATH OF  
EITHER PARTY**

Each party waives and releases all rights, claims, and property interests, of whatever nature, under the present or future laws of Wisconsin or any other jurisdiction, that he or she might otherwise have or acquire as a result of the death of the other party in or to all or any part of the assets classified as the individual property of the other party. This article is intended to apply to all rights and property interests acquired as a result of the parties' marriage including, but not limited to, [rights of intestate succession,]<sup>6</sup> dower and curtesy, rights to elect against the will, election of deferred marital property, election of augmented marital property estate treatment, election against the augmented estate, community property, quasi-community property rights, marital property, and, to the extent permitted by law, spousal support allowances and rights of selection. Neither party shall make or assert any claim or ownership right of any kind in or to the assets classified as the individual property of the other as a result of the death of the other except:

1. Claims for satisfaction of a bona fide debt or to enforce a right under this agreement;

2. Rights to property given or devised to the party by will or transferred to the party by nontestamentary, nonprobate disposition; and

[3. Rights of intestate succession.]<sup>7</sup>

Each party shall join in the execution and filing of any instrument or conveyance and take any other action necessary to relinquish or otherwise avoid the effects of the law of any jurisdiction conferring any such right or interest, if the other party's legal representative or successor in interest so requests. [If either party leaves assets classified as individual property under this agreement passing by the laws of intestate succession of any jurisdiction, those assets shall be distributed

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<sup>6</sup> Delete bracketed language if number 3 is left in.

<sup>7</sup> If the surviving spouse is *not* to receive the individual property described in the agreement if the owner dies intestate, number 3 should be deleted, and the two bracketed sentences dealing with intestacy near the conclusion of Article [VII][VIII] should be left in. If the surviving spouse is to receive the individual property by intestate succession, leave in number 3 and strike the later bracketed sentences.

as if the surviving party had predeceased the deceased party. If necessary, the surviving party shall execute any instrument required to disclaim any assets that would otherwise pass to him or her under the laws of intestate succession.<sup>8</sup>

*[Continue]*

#### **[VIII.][IX.] SCOPE OF AGREEMENT**

This agreement governs certain of the parties' property rights and obligations during the marriage [, upon dissolution of the marriage either by divorce, annulment, legal separation, or other legal proceeding,]<sup>9</sup> and upon the death of either or both of them. [In the event of the dissolution of the parties' marriage by divorce, annulment, legal separation, or other legal proceedings, this agreement shall not affect how the court divides the parties' assets pursuant to section 767.61 of the Wisconsin Statutes or the comparable statute of any applicable jurisdiction.]<sup>10</sup> Except as otherwise necessary to enforce provisions intended to survive dissolution, this agreement is revoked by and shall terminate upon entry of a court judgment of dissolution of the parties' marriage.

#### **[IX.][X.] FINANCIAL DISCLOSURE**

Each party has made [a written] disclosure to the other of his or her property and obligations in connection with the preparation and execution of this agreement. Each party acknowledges receiving such disclosure from the other and represents that his or her own disclosure was fair and reasonable under the circumstances.

#### **[X.][XI.] ENTIRE AGREEMENT**

This agreement represents the entire agreement and understanding between the parties regarding the property and obligations described herein. Both parties acknowledge that neither party has made any conflicting or additional promise or representation to the other regarding any of the subject matter covered by this agreement.

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<sup>8</sup> *See id.*

<sup>9</sup> If optional Article VII is used, the bracketed language in the first sentence of this article should be left in, and the bracketed second sentence should be deleted.

<sup>10</sup> *See id.*

#### **[XI.][XII.] AMENDMENT OR REVOCATION**

This agreement shall not be amended or revoked except by a later marital property agreement.

#### **[XII.][XIII.] BINDING EFFECT**

This agreement shall be binding on the parties and their heirs, legatees, personal representatives, and legal representatives.

#### **[XIII.][XIV.] GOVERNING LAW**

This agreement shall be interpreted in accordance with the laws of the state of Wisconsin, where the parties now reside and are domiciled. The establishment by either or both of the parties of a residence or domicile in another state shall not affect the binding nature or validity of this agreement, the rights of the parties under it, or the laws under which it shall be interpreted.

#### **[XIV.][XV.] CHANGE OF DOMICILE**

If necessary to validate this agreement and make the substance of it enforceable in a jurisdiction in which the parties later become domiciled, the parties (or their legal representatives) agree to reexecute this agreement or one that is in substantially the same form and accomplishes the same objectives, in accordance with the requirements of such jurisdiction.

#### **[XV.][XVI.] SEVERABILITY**

All provisions contained in this agreement are severable. If any of them shall be held to be invalid by any court, this agreement shall be interpreted as if such invalid provisions were not contained herein.<sup>11</sup>

#### **[XVI.][XVII.] REVOCATION OF PRIOR AGREEMENTS**

[By execution of this agreement, the parties revoke each and every marriage agreement, including each and every marital property agreement pursuant to Wisconsin's marital property laws, previously entered into by them that is inconsistent with this agreement. The

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<sup>11</sup> If the invalidity of one provision would make the enforcement of the remainder of this agreement inappropriate, modification of this provision should be considered. *See supra* § 7.70.

parties further agree that any such agreement shall be of no further effect in any respect, as if it had never been entered into.]<sup>12</sup>

### **[XVII.][XVIII.] DEFINITIONS**

Except as otherwise provided in this agreement, the terms *held*, *deferred employment benefit*, *individual property*, and *marital property*<sup>13</sup> shall be interpreted in accordance with and have the incidents provided under the laws of Wisconsin [as amended to date].<sup>14</sup> For purposes of this agreement, individual property also includes individual property under the laws of any other marital property jurisdiction adopting the Uniform Marital Property Act or some variant thereof, separate property under the laws of any community property jurisdiction, and common-law property interests under the laws of any common law jurisdiction. Marital property also includes marital property under the laws of any other jurisdiction adopting the Uniform Marital Property Act or some variant thereof, and community property under the laws of any community property jurisdiction. An asset or assets shall consist of property rights and interests of any nature or description, whether present or future, legal or equitable, vested or contingent, in real or personal property, and shall include assets that either or both of the parties have transferred to a revocable trust of which either or both are the settlor(s).

### **[XVIII.][XIX.] LEGAL REPRESENTATION**

[Before signing this agreement, each party consulted with an attorney of his or her choice.]<sup>15</sup> [The parties are represented by one attorney, and

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<sup>12</sup> Because a limited marital property agreement may be one of a series intended to have cumulative effect or may be a supplement to a more comprehensive marital property agreement, the drafter may wish to delete this article or to substantially modify it to preserve specific portions or features of prior agreements.

<sup>13</sup> Delete any terms not appropriate to the agreement.

<sup>14</sup> See footnote 2 of the marital property agreement at section 7.151, *supra*, for a discussion of the scope of the marital property definition. Use the bracketed language at the end of the sentence if the definitions are to be restricted to the law in effect at the time the agreement is executed. If the definitions are to “float” with the evolution of Wisconsin law following the date of execution of the agreement, the bracketed language should be deleted.

<sup>15</sup> See generally *infra* ch. 14 (separate representation). If this agreement would have a significant impact on the financial position of either of the parties, dual representation may be inappropriate. If optional Article VII (relating to treatment of individual property upon dissolution) is included, dual representation is inappropriate.

they have agreed in writing to such dual representation.]<sup>16</sup> Each party has received from his or her attorney an explanation of the terms and legal significance of this agreement and the effect that it has on any interest that might accrue to each party in property acquired by the other. Each party acknowledges that he or she understands the agreement and its legal effect and is signing the agreement freely and voluntarily.

#### [XIX.][XX.] EFFECTIVE DATE

[This agreement becomes effective upon the marriage of the parties.]  
 [This agreement becomes effective upon the date that both parties are domiciled in Wisconsin.] [This agreement becomes effective upon the later of the marriage of the parties or the date that both parties are domiciled in Wisconsin.] [This agreement becomes effective upon execution.]

Dated: \_\_\_\_\_.

\_\_\_\_\_  
*(party's signature)*

\_\_\_\_\_  
*(party's signature)*

STATE OF WISCONSIN  
 COUNTY OF \_\_\_\_\_

This instrument was acknowledged before me on \_\_\_\_ *(date)* \_\_\_\_ by  
 \_\_\_\_ *(name)* \_\_\_\_ and \_\_\_\_ *(name)* \_\_\_\_.

\_\_\_\_\_  
 Notary Public, State of Wisconsin  
 My commission expires \_\_\_\_\_

*[If a Memorandum of Assets, Liabilities, and Income is to be used, see §§ 7.169 and .172, infra.]*

<sup>16</sup> In the event of a conflict of interest, the consent to dual representation must be in writing after consultation. *See* SCR 20:1.7; *see also infra* ch. 14.



## **D. Sample Agreement to Classify All Property as Individual Property, Terminable by One or Both Spouses [§ 7.158]**

### **1. Introduction [§ 7.159]**

The primary purpose of this agreement is to classify all of the spouses' property as individual property, but to permit either spouse unilaterally to cause the spouses' property regime to revert to that which would apply in the absence of the agreement. The agreement has been drafted for persons who are married to each other. If the form is to be used by parties who intend to marry, it may be modified accordingly. By its terms, it is not intended to affect the division of the spouses' assets in the event of the dissolution of their marriage. One of its advantages is that, in appropriate circumstances, it may permit the spouses to be represented by a single attorney. *See infra* ch. 14. Similarly, it may permit less detailed financial disclosures than might otherwise be required. A severability provision, *see supra* § 7.70, has not been included because of the likelihood that the spouses would not wish to have the agreement at all if one of its key provisions (such as the elective right of either spouse to change the property classification system) were found to be invalid. It is a sample form only and does not purport to be all-inclusive. With respect to the methods by which spouses may classify or reclassify property, see section 766.31(10) and chapter 2, *supra*. See chapters 9 and 10, *infra*, for tax and estate planning considerations, respectively. Marital property agreements must be tailored to the parties' circumstances, and tax issues must be carefully considered. For other resources concerning the drafting of provisions for marital property agreements, see section 7.109, *supra*.

### **2. Form [§ 7.160]**

#### **MARITAL PROPERTY AGREEMENT**

This is a marital property agreement between     (husband)     and     (wife)    , husband and wife, of \_\_\_\_\_ County, Wisconsin.

WHEREAS, the parties desire by this agreement to determine the system of property classification and ownership applicable during their marriage and upon termination of their marriage by the death of one or

both of the parties, both as to assets that they now own and as to those they hereafter acquire;

WHEREAS, each party has made and acknowledges receiving a fair and reasonable disclosure under the circumstances of the parties' property and financial obligations<sup>1</sup> [, as set forth in a separate Memorandum of Assets, Liabilities, and Income executed by them on this date];

WHEREAS, each party understands that in the absence of this agreement the law would confer upon him or her property rights and interests in certain of the present and future assets possessed or acquired by the other, and each party further understands that those rights and interests will be affected by this agreement;

WHEREAS, the parties desire to classify, pursuant to Wisconsin law, all assets of either or both of them as individual property and none as marital property except as otherwise specifically provided in this agreement;

WHEREAS, the parties further desire to provide that all obligations now outstanding and hereafter incurred by either of them shall be their respective sole obligations, as if they were unmarried persons;

NOW, THEREFORE, it is agreed as follows:

## **I. ALL PROPERTY IS INDIVIDUAL PROPERTY**

**A.** The parties agree that all of the assets of either or both of them shall be classified as individual property and none of their assets shall be classified as marital property except as otherwise provided in this agreement. In carrying out this intention, the following rules shall apply:

**1.** An asset now or hereafter held by a party shall be classified as that party's individual property.

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<sup>1</sup> There are no court decisions under the Act as to what constitutes a "fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations" for purposes of enforceability under section 766.58(6)(c). Inferentially, the financial disclosure statements that are included as part of the statutory terminable marital property classification agreement and the statutory terminable individual property classification agreement, *see infra* §§ 7.175, .178, should be sufficient. The memoranda of assets, liabilities, and income at sections 7.169 and .172, *infra*, should also be sufficient because they provide even greater detail than the statutory financial disclosure forms.

**2.** Unless expressly provided to the contrary in a document of title or other writing signed by both parties, an asset now or hereafter held by both parties shall be classified as the individual property of both parties as joint tenants with right of survivorship and shall have all of the incidents of such tenancy.

**3.** An asset not held by a party shall be classified as the individual property of a party to the extent that the party (a) furnished the consideration in money or money's worth (including the incurring of a debt) for the asset; or (b) received the asset by gift, inheritance, nontestamentary transfer, or trust distribution. The parties recognize that assets acquired as described in (a) and (b) above may be co-owned as individual property. The parties further agree that when one party furnishes the consideration for an asset that he or she gives to the other party, the asset is the individual property of the donee party.

**B.** The classification of an asset as individual property shall extend to the income from the asset; to the realized or unrealized appreciation in the value of the asset regardless of whether the appreciation occurred through general market conditions or through the application of labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity by either of the parties; and to property received in exchange for or with the proceeds of the asset. The classification of an asset held by one or both of the parties shall not be affected by the classification of property added to or mixed with the asset, and any such addition or mixing shall be deemed a gift to the holding party or parties.

**C.** The parties agree that they shall not acquire any marital property until such time as the right granted under Article IV of this agreement is exercised, if ever.

**D.** The parties agree that:

**1.** If the parties are domiciled in Wisconsin at the death of the first of them to die, only the elective rights in Article[s] [IV and V] [IV] shall apply, and each party waives any statutory deferred marital property elective rights in and to assets classified as individual property under this agreement.

**2.** If the parties are domiciled in another community property jurisdiction at the death of the first of them to die, only the elective rights in Article[s] [IV and V] [IV] shall apply, and each party waives any quasi-community property or other elective rights in and to assets classified as individual property under this agreement.

3. If the parties are domiciled in a common law jurisdiction at the death of the first of them to die, the surviving spouse shall have either the elective rights in Article[s] [IV and V] [IV] or any elective rights the surviving spouse may have under the laws of the common law jurisdiction that are applicable to the assets of the deceased party, but not both.

## **II. MANAGEMENT AND CONTROL**

Each party shall have the full and exclusive power of management and control over his or her individual property, free from any interference or claims by the other party. Each party shall have the unqualified right to dispose of his or her individual property at any time by sale, exchange, gift, disposition at death, or otherwise, to any person or persons he or she may choose, including the other party, without the other party's consent.

## **III. OBLIGATIONS AND CREDITORS<sup>2</sup>**

A. Except for obligations for normal support and maintenance, all other obligations, including but not limited to contractual obligations and those for torts, punitive damages, penalties, fines, or forfeitures that either party has incurred or hereafter incurs, and the parties' respective shares of obligations that have been or may be incurred jointly, either with each other or with third persons, shall be the obligation of the incurring party as though he or she were an unmarried person, regardless of when the obligation is incurred. Unless prohibited by law, any such obligation shall be satisfied exclusively out of the individual property of the incurring party as defined by this agreement. If a creditor obtains payment or satisfaction in connection with the obligation of a party out of the individual property of the other party as defined by this agreement, the other party shall be entitled to full reimbursement from the incurring party or his or her estate.

B. Each party shall provide all prospective credit grantors (except those for normal support) with a copy of this agreement before credit is granted or an open-end credit plan is entered into.

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<sup>2</sup> See Article III of the marital property agreement at section 7.154, *supra*, for additional and alternative clauses dealing with obligations and creditors.

[Choose appropriate alternative]<sup>3</sup>

[Alternative I]

#### **IV. ELECTIVE RIGHT TO PROSPECTIVELY CHANGE PROPERTY CLASSIFICATION SYSTEM**

Either party may at any time during the marriage cause a change from the property classification system in Article I to that which would apply to the parties' property in the jurisdiction or jurisdictions where the parties are domiciled on and after the effective date of the change. The change shall be prospective only and shall not alter the classification of, or the rights of the parties in or with respect to, the individual property owned or acquired by either party before such change. The change shall be accomplished by delivery of a notice in substantially the form of attached Exhibit A by the invoking party to the other. The effective date of the change shall be 30 days from the date the notice is delivered. The parties understand and specifically intend that the terms of this article give each party acting alone the right to cause a prospective change in their property rights. The exercise of that right shall not be an amendment or revocation of this agreement. This agreement shall continue in full force and effect following any such exercise until amended or revoked by the parties as provided in Article [VIII][IX].

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<sup>3</sup> If the right to change from the individual property classification system spelled out in the agreement is to be prospective only, Alternative I should be used. If the right to change is to be completely retroactive, Alternative II should be used. It may be fairer to allow full retroactivity, except for gifts to third persons (such gifts could be made subject to a good-faith standard). Moreover, if the agreement is fully retroactive, a death-bed election to change the property classification system may create a larger body of marital property assets that would qualify for a full adjustment in basis at the death of the first spouse to die. On the other hand, questions as to whether the agreement is illusory may arise in situations in which one spouse alone is permitted to effectively rescind the agreement on a retroactive basis. *See supra* § 7.117.

Permitting only a prospective change in the property classification system adopted by the agreement increases the likelihood that separate representation may be required if the agreement would have a significant impact on the financial position of either of the parties. On the other hand, making the right to change prospective only has the advantage that it is consistent with the format used in the statutory terminable individual property classification agreement in section 766.589. *See supra* §§ 7.73–82.

**V. ELECTIVE RIGHT AT DEATH OF A PARTY**

**A.** If one party dies while married to the other, the surviving party shall have an elective right to an amount equal to the excess, if any, of (1) the value of all property that the surviving party would have owned if Wisconsin's marital property laws, as amended to date and from time to time hereafter, had been in effect throughout their marriage and no property had passed to the surviving party from the deceased party by will, trust, beneficiary designation, annuity, or otherwise as a result of the deceased party's death, over (2) the value of the property actually owned by the surviving party immediately following the deceased party's death, including that passing to the surviving party from the deceased party. For purposes of (2) above, property passing to the surviving party or to a trustee from the deceased party shall be treated as owned by the surviving party if the property qualifies for the federal estate tax marital deduction under section 2056 of the Internal Revenue Code as amended.<sup>4</sup>

**B.** For purposes of this article, all survivorship requirements of less than six months shall be deemed to have been satisfied and any statutory elective rights exercised by the survivor shall be deemed to have been exercised immediately following the deceased party's death. All values shall be determined as of the deceased party's date of death.

**C.** The surviving party may assert his or her elective right under this article in whole or in part at any time before the first to occur of the following:

1. The expiration of six months following the death of the predeceasing party;
2. The last date for filing claims under the applicable statute governing claims based on a marital property agreement; or
3. The death of the surviving party.

The elective right shall be satisfied first and to the greatest extent possible out of the deceased party's probate estate. Each party understands that in order to enforce this contractual right, he or she may

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<sup>4</sup> This sentence has the effect of permitting property passing into a qualified terminable interest property (QTIP) trust for the benefit of a surviving spouse to be counted against the amount available for election. This provision may be more restrictive than the statutory provisions for satisfaction of the deferred marital property elective share. *See, e.g.*, Wis. Stat. §§ 861.02–.06.

be required to comply with the claim-filing requirements of the probate laws governing the deceased party's estate. The parties agree that a contingent claim for the maximum amount under this article shall be sufficient if asserted in general terms that apprise the personal representative(s) of the deceased party's estate of the nature and extent of the claim. If the full amount of the elective right asserted by the surviving party cannot be satisfied out of the deceased party's probate estate, the parties agree that the surviving party shall have a pro rata ownership interest in all of the deceased party's nonprobate assets that are includible in the deceased party's gross estate for federal estate tax purposes sufficient to satisfy the balance of the elective right. If the reason that the elective right asserted by the surviving party cannot be satisfied out of the deceased party's probate estate is the failure by the surviving party to file a claim against the deceased party's probate estate within the period of time allowed by applicable law, the amount of the asserted elective right shall be reduced by the amount that could have been satisfied out of the deceased party's probate estate had a timely claim been filed.

**D.** If the surviving party exercises the elective right in whole or in part, the parties agree that the exercise of the election shall constitute a disclaimer by the surviving party of any provisions made for the surviving party in the will or any revocable trust of the deceased party, and the surviving party shall execute such documents and take such actions as are required to effect such disclaimer as a condition of the exercise of such election.

*[Or]*

*[Alternative II]*

#### **IV. ELECTIVE RIGHT TO RETROACTIVELY CHANGE PROPERTY CLASSIFICATION SYSTEM**

**A.** Either party at any time during the marriage, or if the marriage ends by the death of one of the parties, the surviving party, may elect the alternative rights in this article in lieu of the rights conferred on the electing party in other articles of this agreement. If one of the parties elects the rights conferred by this article, both parties shall forfeit the provisions made in the other articles in this agreement, and such provisions shall be unenforceable by either party. If one of the parties elects the rights conferred by this article during the parties' marriage, both the electing party and the other party shall have the rights conferred by this article in lieu of any rights conferred on the parties in other articles of this agreement. The parties understand and specifically intend that the terms of this article give each party acting alone the right to cause a

retroactive change in their property rights. The exercise of that right shall not be an amendment or revocation of this agreement. This agreement shall continue in full force and effect following any such exercise until otherwise amended or revoked as provided in this agreement.

**B.** If an election of the alternative rights in this article is made during the lifetimes of both parties, then the following shall occur:

1. All of the property that at the time of the election would have been marital property of the parties if this agreement had not been entered into shall be reclassified as marital property by virtue of this agreement and without the necessity of further agreement between the parties or further action by either party. Both parties agree to take such action and execute such documents as may be required to confirm such reclassification.

2. Upon the death of the first of the parties to die, all of the property of the deceased party that at the death of the deceased party would have been subject to any rights of the surviving spouse conferred by operation of law if this agreement had not been entered into, including the deferred marital property and the augmented marital property estate elective rights, shall be subject to the elective right of the surviving party described in Paragraph D of this article. All other property of the deceased party shall be classified as the individual property of the deceased party.

**C.** If the election of the alternative rights in this article is made after the death of the one of the parties, then the following shall occur:

1. All of the property that at the time of the election would have been marital property of the parties if the parties were then living and if this agreement had not been entered into shall be divided into two equal shares. One share shall be paid and distributed to the surviving party, and the other share shall be paid and distributed to the deceased party's estate.

2. All of the property of the deceased party that at the death of the deceased party would have been subject to any rights of the surviving spouse conferred by operation of law if this agreement had not been entered into, including the deferred marital property and augmented marital property estate elective rights, shall be subject to the elective right of the surviving party described in Paragraph D of this article. All other property of the deceased party shall be classified as the individual property of the deceased party.



**D.** The elective right of the surviving party referred to in Paragraphs B.2. and C.2. of this article shall be a right to receive property following the deceased party's death that is equal in amount to the property that would have been received under the rights of the surviving spouse conferred by operation of law if this agreement had not been entered into, including the rights granted to the surviving spouse with respect to the deferred marital property and augmented marital property estate elections under chapters 766 and 861 of the Wisconsin Statutes or any successor statutes in effect at the time of the first party's death. This elective right shall be subject to bar and to reduction in the same manner and to the same extent that would have applied to the rights of the surviving spouse conferred by operation of law if this agreement had not been entered into, including the rights with respect to the deferred marital property and augmented marital property estate elections under chapters 766 and 861 of the Wisconsin Statutes, or any successor statutes in effect at the time of the first party's death.

**E.** The election of the alternative rights conferred by this article shall be accomplished by execution by one of the parties of a notice making specific reference to this article and by delivery of such notice (1) within five days of execution to the other party, if living, or (2) if not living, to the personal representative of the other party's estate, within the time period specified below. Following the death of a party, the surviving party may assert his or her elective right under this article in whole or in part at any time before the first to occur of the following:

1. The expiration of six months following the death of the predeceasing party;
2. The last date for filing claims under the applicable statute governing claims based on a marital property agreement; or
3. The death of the surviving party.

All values shall be determined as of the deceased party's date of death. The elective rights shall be satisfied first and to the greatest extent possible out of the deceased party's probate estate. Each party understands that in order to enforce this contractual right, he or she may be required to comply with the claim-filing requirements of the probate laws governing the deceased party's estate. The parties agree that a contingent claim for the maximum amount under this article shall be sufficient if asserted in general terms that apprise the personal representative(s) of the deceased party's estate of the nature and extent of the claim. If the surviving party exercises the elective right in whole or in part, the parties agree that the exercise of the election shall constitute a disclaimer by the surviving party of any provisions made for the

surviving party in the will or any revocable trust of the deceased party, and the surviving party shall execute such documents and take such actions as are required to effect such disclaimer as a condition of the exercise of such election.

*[Continue]*

**[V.][VI.] AGREEMENT NOT TO AFFECT PROPERTY DIVISION IN  
EVENT OF DISSOLUTION**

In the event of the dissolution of the parties' marriage by divorce, annulment, legal separation, or other legal proceeding, this agreement shall not affect how the court divides the parties' assets, pursuant to section 767.61 of the Wisconsin Statutes or the comparable statute of any applicable jurisdiction. Except as otherwise necessary to enforce provisions intended to survive a dissolution, this agreement is revoked by and shall terminate upon entry of a court judgment of dissolution of the parties' marriage.

**[VI][VII.] FINANCIAL DISCLOSURE**

Each party has made [a written] disclosure to the other of his or her property and obligations in connection with the preparation and execution of this agreement. Each party acknowledges receiving such disclosure from the other and represents that his or her own disclosure was fair and reasonable under the circumstances.

**[VII.][VIII] ENTIRE AGREEMENT**

This agreement represents the entire agreement and understanding between the parties regarding the property and obligations described herein. Both parties acknowledge that neither party has made any conflicting or additional promise or representation to the other regarding any of the subject matter covered by this agreement.

**[VIII.][IX.] AMENDMENT OR REVOCATION**

This agreement shall not be amended or revoked except by a later marital property agreement.

**[IX.][X.] BINDING EFFECT**

This agreement shall be binding on the parties, their heirs, legatees, personal representatives, and legal representatives.

## **[X.][XI.] GOVERNING LAW**

This agreement shall be interpreted in accordance with the laws of the state of Wisconsin, where the parties now reside and are domiciled. The establishment by either or both of the parties of a domicile in another state shall not affect the binding nature or validity of this agreement, the rights of the parties under it, or the laws under which it shall be interpreted.

## **[XI.][XII.] CHANGE OF DOMICILE**

If necessary to validate this agreement and make the substance of it enforceable in a jurisdiction in which the parties later become domiciled, the parties (or their legal representatives) agree to reexecute this agreement or one that is in substantially the same form and accomplishes the same objectives, all in accordance with the requirements of such jurisdiction.

## **[XII.][XIII.] REVOCATION OF PRIOR AGREEMENTS**

By execution of this agreement, the parties revoke each and every marriage agreement previously entered into by them, including each and every marital property agreement pursuant to Wisconsin's marital property laws. The parties further agree that any such agreement shall be of no further force and effect in any respect, as if it had never been entered into.<sup>5</sup>

## **[XIII.][XIV.] DEFINITIONS**

Except as otherwise provided in this agreement, the terms *held*, *individual property*, *marital property*, and *deferred employment benefit* shall be interpreted in accordance with and have the incidents provided under the laws of Wisconsin [as amended to date].<sup>6</sup> For purposes of this agreement, individual property also includes individual property under the laws of any other jurisdiction adopting the Uniform Marital Property

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<sup>5</sup> Note that if certain actions taken or certain property classifications established by earlier agreements are to be preserved, special provisions should be included for that purpose.

<sup>6</sup> See footnote 2 of the marital property agreement at section 7.151, *supra*, for a discussion of the scope of the marital property definition. Use the bracketed language at the end of the sentence if the definitions are to be restricted to the law in effect at the time the agreement is executed. If the definitions are to “float” with the evolution of Wisconsin law following the date of execution of the agreement, the bracketed language should be deleted.

Act or some variant thereof, separate property under the laws of any community property jurisdiction, and common law property interests under the laws of any common law jurisdiction. Marital property also includes marital property under the laws of any other jurisdiction adopting the Uniform Marital Property Act or some variant thereof and community property under the laws of any community property jurisdiction. An *asset* or *assets* shall consist of property rights and interests of any nature or description, whether present or future, legal or equitable, vested or contingent, in real or personal property, and shall include assets that either or both of the parties have transferred to a revocable trust of which either or both are the settlor(s).

#### **[XIV.][XV.] LEGAL REPRESENTATION**

[Before signing this agreement, each party consulted with an attorney of his or her choice.]<sup>7</sup> [The parties are represented by one attorney in connection with this agreement, and each has agreed in writing to such dual representation.]<sup>8</sup> Each party has received from his or her attorney an explanation of the terms and legal significance of this agreement and the effects it will have on the property and rights of the parties, as well as an explanation of the marital property system that would apply under present Wisconsin law in the absence of this agreement. Each party acknowledges that he or she understands this agreement and its legal effect and is signing voluntarily.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
(party's signature)

\_\_\_\_\_  
(party's signature)

STATE OF WISCONSIN  
COUNTY OF \_\_\_\_\_

This instrument was acknowledged before me on     (date)     by  
    (name)     and     (name)    .

\_\_\_\_\_  
Notary Public, State of Wisconsin  
My commission expires \_\_\_\_\_

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<sup>7</sup> See generally *infra* ch. 14 (separate representation).

<sup>8</sup> In the event of a conflict of interest, the consent to dual representation must be in writing after consultation. See SCR 20:1.7; see also *infra* ch. 14.

*[If a Memorandum of Assets, Liabilities, and Income is to be used, see sections 7.169 and .172, infra.]*

*[Include if appropriate]*

**EXHIBIT A<sup>9</sup>**

**NOTICE OF ELECTION TO PROSPECTIVELY CHANGE PROPERTY CLASSIFICATION**

Pursuant to Article IV of a marital property agreement dated \_\_\_\_\_, between my spouse, \_\_\_\_\_, and me, I elect to change the property classification provided in Article I of that agreement to that which would apply to our property in the jurisdiction or jurisdictions in which my spouse and I are domiciled on and after the effective date of this election. This change shall be effective 30 days from the date this notice is delivered to my spouse.

Dated: \_\_\_\_\_.

\_\_\_\_\_

**ACKNOWLEDGMENT OF DELIVERY**

I acknowledge that a copy of the foregoing Notice of Election to Prospectively Change Property Classification was delivered to me on \_\_\_\_\_.

\_\_\_\_\_

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<sup>9</sup> Include Exhibit A only if Alternative I, *supra*, is selected.

## E. Sample Will Substitute Agreement [§ 7.161]

### 1. Introduction [§ 7.162]

The primary purpose of this agreement is to transfer all marital, individual, and predetermination date property owned by a deceased spouse to the surviving spouse without probate by nontestamentary disposition pursuant to section 766.58(3)(f). This sample agreement does not govern disposition at the death of the surviving spouse and thus leaves the surviving spouse free to dispose of the property as he or she desires after the death of the first spouse to die. See footnote 4, *infra*, regarding provisions intended to operate at the deaths of both spouses. If the spouses also desire to reclassify most or all of their property as marital property, the appropriate recital clauses and the operative language of Article I from the sample agreement in section 7.151, *supra*, might be included. The agreement applies only to property that would otherwise be subject to administration; it does not purport to transfer nonprobate assets because of the possibility of conflicts with outstanding beneficiary designations or other nonprobate transfer arrangements. See *supra* §§ 7.102–.104. This agreement has been drafted for persons who are married to each other. If the form is to be used by parties who intend to marry, it may be modified accordingly. The agreement is a sample form only and does not purport to be all-inclusive. Marital property agreements must be tailored to the parties' circumstances, and tax issues must be carefully considered. For other resources concerning the drafting of provisions for marital property agreements, see section 7.109, *supra*.

### 2. Form [§ 7.163]

#### MARITAL PROPERTY AGREEMENT

This is a marital property agreement between \_\_\_\_\_ and \_\_\_\_\_, husband and wife, of \_\_\_\_\_ County, Wisconsin.

WHEREAS, the parties are presently married to each other, and each desires to dispose of all property that would otherwise be subject to probate administration and that he or she owns at the death of the first of

them, without probate by nontestamentary disposition and without any intention to revoke the will of either party;<sup>1</sup>

WHEREAS, each party has made and acknowledges receiving fair and reasonable disclosure under the circumstances of the parties' property and financial obligations<sup>2</sup> [, as set forth in a separate Memorandum of Assets, Liabilities, and Income executed by them on this date];

WHEREAS, the parties desire to avail themselves of the right contained in section 766.58(3)(f) of the Wisconsin Statutes to dispose of the marital property, individual property, and predetermination date property that each of them now owns or hereafter acquires to the survivor by nontestamentary disposition upon the death of the first of them to die;

NOW, THEREFORE, it is agreed as follows:

## **I. SCOPE OF AGREEMENT**

This agreement applies to the interest of both parties in assets classified as marital property and in assets other than marital property owned by the parties at the death of the first of the parties to die.

## **II. TRANSFER OF ASSETS WITHOUT PROBATE UPON DEATH OF A PARTY**

Upon the death of either of the parties, all of the decedent's ownership interests in assets described and classified in Article I that in

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<sup>1</sup> A marital property agreement ordinarily will not suffice to revoke a will, either expressly or by inconsistency, unless executed with all the formalities of a will. Wis. Stat. § 853.11(1). However, a will substitute agreement may dispose of all assets that otherwise would be subject to probate at the death of the first spouse to die, thus having the same practical consequence as a revocation of the will.

<sup>2</sup> There are no court decisions under the Act as to what constitutes a "fair and reasonable disclosure, under the circumstances, of the other spouse's property or financial obligations" for purposes of enforceability under section 766.58(6)(c). Inferentially, the financial disclosure statements that are included as part of the statutory terminable marital property classification agreement and the statutory terminable individual property classification agreement, *see infra* §§ 7.175, .178, should be sufficient. The memoranda of assets, liabilities, and income at sections 7.169 and .172, *infra*, should also be sufficient because they provide even greater detail than the statutory financial disclosure forms.

the absence of this agreement would be subject to probate, shall immediately pass to and vest in the survivor without probate by nontestamentary disposition.<sup>3</sup> This article is intended to be a disposition of property as described in section 766.58(3)(f) of the Wisconsin Statutes.

### **III. REVOCATION UPON DISSOLUTION OF MARRIAGE**

Except as otherwise necessary to enforce provisions intended to survive dissolution, this agreement is revoked by and shall terminate upon entry of a court judgment of dissolution of the parties' marriage.

### **IV. CHANGE OF DOMICILE**

This agreement is revoked and shall terminate at such time as either or both of the parties establish a domicile in another state.<sup>4</sup>

### **V. FINANCIAL DISCLOSURE**

Each party has made [a written] disclosure to the other of his or her property and obligations in connection with the preparation and execution of this agreement. Each party acknowledges receiving that disclosure from the other and represents that his or her own disclosure was fair and reasonable under the circumstances.

### **VI. AMENDMENT OR REVOCATION**

This agreement may be amended or revoked only by a later written marital property agreement.

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<sup>3</sup> For an example of a will substitute provision that operates at the deaths of both spouses, see Article VI of the opt-in marital property agreement at section 7.151, *supra*. These provisions envisage transfers of assets to a jointly created revocable trust. Consistent with section 766.58(3)(f), these provisions specifically permit the surviving spouse to amend the will substitute agreement with regard to the property to be disposed of at his or her death. This right to amend may be restricted if the agreement expressly so provides or if the property is held in trust expressly established under the agreement. *See supra* § 7.100. If a restrictive provision of this sort is used, the final "whereas" clause in the recitals of this agreement should be modified appropriately.

<sup>4</sup> It would appear that many states would not recognize an agreement of this kind as a will substitute, particularly with respect to property acquired after either or both of the spouses change their domicile to that state. Exceptions are Washington, Idaho, Texas, and perhaps states that have enacted Uniform Probate Code § 6-201.



## VII. BINDING EFFECT

This agreement shall be binding on the parties, their heirs, legatees, personal representatives, and legal representatives.

## VIII. GOVERNING LAW

This agreement shall be interpreted in accordance with the laws of the state of Wisconsin, where the parties now reside and are domiciled.

## IX. DEFINITIONS

Except as otherwise provided in this agreement, the terms *held*, *individual property*, and *marital property* shall be interpreted in accordance with and have the incidents provided under the laws of Wisconsin [as amended to date.]<sup>5</sup> An *asset* or *assets* shall consist of property rights and interests of any nature or description, whether present or future, legal or equitable, vested or contingent, in real or personal property, and shall include assets that either or both of the parties have transferred to a revocable trust of which either or both are the settlor(s).

## X. LEGAL REPRESENTATION

[Before signing this agreement, each party consulted with an attorney of his or her choice.]<sup>6</sup> [The parties are represented by one attorney in connection with this agreement, and each has agreed in writing to such dual representation.]<sup>7</sup> Each party has received from his or her attorney an explanation of the terms and legal significance of this agreement. Each party acknowledges that he or she understands this agreement and its legal effect and is signing voluntarily.

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<sup>5</sup> See footnote 2 of the marital property agreement at section 7.151, *supra*, for a discussion of the scope of the marital property definition. Use the bracketed language at the end of the sentence if the definitions are to be restricted to the law in effect at the time the agreement is executed. If the definitions are to “float” with the evolution of Wisconsin law following the date of execution of the agreement, the bracketed language should be deleted.

<sup>6</sup> See generally *infra* ch. 14 (separate representation).

<sup>7</sup> In the event of a conflict of interest, the consent to dual representation must be in writing after consultation. See SCR 20:1.7; see also *infra* ch. 14.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
*(party's signature)*

\_\_\_\_\_  
*(party's signature)*

STATE OF WISCONSIN  
COUNTY OF \_\_\_\_\_

This instrument was acknowledged before me on     (date)     by  
    (name)     and     (name)    .

\_\_\_\_\_  
Notary Public, State of Wisconsin  
My commission expires \_\_\_\_\_

*[If a Memorandum of Assets, Liabilities, and Income, is to be used, see  
sections 7.169 and .172, infra.]*

## **F. Sample Revocation of Prior Marital Property Agreements [§ 7.164]**

### **1. Introduction [§ 7.165]**

The purpose of this agreement is to revoke all prior marriage agreements and marital property agreements in a manner consistent with the requirements of section 766.58(4). One reason to revoke prior agreements is to ensure that forgotten earlier agreements do not jeopardize the current estate plan. Similar revocation language is also used in the agreement forms in sections 7.151–.163, *supra*. The following is a sample form only and does not purport to be all-inclusive.

### **2. Form [§ 7.166]**

#### **MARITAL PROPERTY AGREEMENT**

This is a marital property agreement between \_\_\_\_\_ and \_\_\_\_\_, husband and wife, of \_\_\_\_\_ County, Wisconsin.

WHEREAS, each party has made and acknowledges receiving fair and reasonable disclosure under the circumstances of the parties' property and financial obligations<sup>1</sup> [ , as set forth in a separate Memorandum of Assets, Liabilities, and Income executed by them on this date];

NOW, THEREFORE, it is agreed as follows:

#### **I. REVOCATION OF PRIOR AGREEMENTS**

By execution of this agreement, the parties revoke each and every marriage agreement previously entered into by them, including each and

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<sup>1</sup> There are no court decisions under the Act as to what constitutes a “fair and reasonable disclosure, under the circumstances, of the other spouse’s property or financial obligations” for purposes of enforceability under section 766.58(6)(c). Inferentially, the financial disclosure statements that are included as part of the statutory terminable marital property classification agreement and the statutory terminable individual property classification agreement, *see infra* §§ 7.175, .17, should be sufficient. The memoranda of assets, liabilities, and income at sections 7.169 and .172, *infra*, should also be sufficient because they provide even greater detail than the statutory financial disclosure forms.

every marital property agreement pursuant to Wisconsin's marital property laws. The parties further agree that any such agreement shall be of no further force and effect in any respect, as if it had never been entered into.<sup>2</sup>

## **II. FINANCIAL DISCLOSURE**

The parties agree that the disclosures of assets, liabilities, and income that they have made to each other in connection with this agreement are fair and reasonable disclosures of each other's property and financial obligations.

## **III. AMENDMENT OR REVOCATION**

This agreement (including this agreement against oral modification or waiver) shall not be modified or waived except by a later marital property agreement.

## **IV. BINDING EFFECT**

This agreement shall be binding on the parties, their heirs, legatees, personal representatives, and legal representatives.

## **V. GOVERNING LAW**

This agreement shall be interpreted in accordance with the laws of the state of Wisconsin, where the parties now reside and are domiciled. The establishment by either or both of the parties of a domicile in another state shall not affect the binding nature or validity of this agreement, the rights of the parties under it, or the laws under which it shall be interpreted.

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<sup>2</sup> To the extent practicable, it is desirable to specifically identify each agreement that is revoked. Also note that if certain actions taken or certain property classifications established by earlier agreements are to be preserved, special provisions should be included for that purpose, or a separate marital property agreement should be prepared.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
(party's signature)

\_\_\_\_\_  
(party's signature)

STATE OF WISCONSIN  
COUNTY OF \_\_\_\_\_

This instrument was acknowledged before me on     (date)     by  
    (name)     and     (name)    .

\_\_\_\_\_  
Notary Public, State of Wisconsin  
My commission expires \_\_\_\_\_

*[If a Memorandum of Assets, Liabilities, and Income is to be used, see  
sections 7.169, .172, infra.]*

## **G. Sample Memorandum of Assets, Liabilities, and Income (Asset Disclosure by Classification) [§ 7.167]**

### **1. Introduction [§ 7.168]**

The purpose of this Memorandum of Assets, Liabilities, and Income is to provide a framework for memorializing the parties' disclosures in a manner that will meet the fair and reasonable disclosure requirements of section 766.58(6)(c)1. It is a sample form only, and in some instances attachment of schedules listing one or more categories of assets or liabilities in greater detail may be appropriate.

### **2. Form [§ 7.169]**

#### **MEMORANDUM OF ASSETS, LIABILITIES, AND INCOME**

This memorandum contains a fair and reasonable disclosure of our property and financial obligations at approximate fair market values that we believe to be accurate and correct. We understand and agree that this memorandum has been prepared in connection with a marital property agreement executed by us on this date.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
*(party's signature)*

\_\_\_\_\_  
*(party's signature)*

#### **Assets and Liabilities**

Property acquired before the determination date (January 1, 1986, for married persons resident in Wisconsin at that time) in one of our names is listed entirely in the predetermination date property column of the spouse who owns it. Predetermination date property owned by us as tenants in common is listed half in the husband's column and half in the wife's column, and mortgages against that property are divided equally. Property acquired after the determination date that is owned as individual property is listed entirely in the individual property column of the spouse who owns it. Property acquired after the determination date that is owned as marital property is listed half in the husband's column and half in the wife's column under marital property. Property owned by us in a

predetermination date joint tenancy with right of survivorship or as survivorship marital property acquired after the determination date is listed half in the husband's column and half in the wife's column under joint tenancy and survivorship marital property, and mortgages against that property are divided equally.

Unsecured debts or obligations incurred before the determination date and any premarital debts are shown in the predetermination date property column of the spouse who incurred the debt. Unsecured debts or obligations incurred after the determination date in the interest of the marriage and the family (family purpose debts) are shown entirely in the marital property column of the spouse who incurred the debt, even though marital property interests of the other spouse may be reached to satisfy these obligations. Unsecured non-family purpose debts or obligations incurred after the determination date are shown in the individual property column of the spouse who incurred them.

	Husband			
	Predeter- mination Date Property <sup>1</sup>	Individual Property	Marital Property <sup>2</sup> (1/2 only)	Joint Tenancy and Survivorship Marital Property (1/2 only)
Principal residence (Less mortgage)	\$ _____ (_____)	\$ _____ (_____)	\$ _____ (_____)	\$ _____ (_____)
Other residential property in Wisconsin (Less mortgage)	(_____)	(_____)	(_____)	(_____)
Other residential property not in Wisconsin (Less mortgage)	(_____)	(_____)	(_____)	(_____)
Investment real estate in Wisconsin (Less mortgage)	(_____)	(_____)	(_____)	(_____)
Investment real estate not in Wisconsin (Less mortgage)	(_____)	(_____)	(_____)	(_____)
Stock in closely held corporations	_____	_____	_____	_____
Partnership interests	_____	_____	_____	_____
Marketable stocks and bonds	_____	_____	_____	_____
Cash, checking accounts, savings accounts, savings bonds, and money market investments	_____	_____	_____	_____
Notes, mortgages, and land contracts	_____	_____	_____	_____
Automobiles, boats, snowmobiles, and airplanes	_____	_____	_____	_____
Antiques, collections, art, jewelry	_____	_____	_____	_____
Other household furnishings	_____	_____	_____	_____
Other significant property	_____	_____	_____	_____
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____
Property held in revocable trusts (describe)	_____	_____	_____	_____
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____



**Husband**

	<u>Predeter- mination Date Property<sup>1</sup></u>	<u>Individual Property</u>	<u>Marital Property<sup>2</sup> (1/2 only)</u>	<u>Joint Tenancy and Survivorship Marital Property (1/2 only)</u>
Other interests in trusts (describe whether income or principal, mandatory or discretionary, termina- tion date(s), approximate value of trust assets)				
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____
Secured debts other than mortgages deducted above (indicate security)				
_____	(_____)	(_____)	(_____)	(_____)
_____	(_____)	(_____)	(_____)	(_____)
Unsecured debts				
_____	(_____)	(_____)	(_____)	
_____	(_____)	(_____)	(_____)	
Death value of pension, profit- sharing, and other employ- ment benefits (Beneficiary _____)	_____	_____	_____	
Death value of HR-10 and IRA accounts (Beneficiary _____)	_____	_____	_____	

Life insurance on life of husband	<u>Face Amount</u>	<u>Current Cash Value<sup>4</sup></u>
1. Owned by husband <sup>3</sup> (Beneficiary _____)	\$ _____	\$ _____
2. Owned by wife (Beneficiary _____)	_____	_____
3. Owned by someone else (Beneficiary _____)	_____	_____

Life insurance on life of another	<u>Face Amount</u>	<u>Current Cash Value<sup>4</sup></u>	<u>Person Insured</u>
Owned by husband <sup>3</sup> (Beneficiary _____)	\$ _____	\$ _____	\$ _____

**Wife**

	<u>Predeter- mination Date Property<sup>1</sup></u>	<u>Individual Property</u>	<u>Marital Property<sup>2</sup> (1/2 only)</u>	<u>Joint Tenancy and Survivorship Marital Property (1/2 only)</u>
Principal residence (Less mortgage)	\$ _____	\$ _____	\$ _____	\$ _____
Other residential property in Wisconsin (Less mortgage)	_____	_____	_____	_____
Other residential property not in Wisconsin (Less mortgage)	_____	_____	_____	_____
Investment real estate in Wisconsin (Less mortgage)	_____	_____	_____	_____
Investment real estate not in Wisconsin (Less mortgage)	_____	_____	_____	_____
Stock in closely held corporations	_____	_____	_____	_____
Partnership interests	_____	_____	_____	_____
Marketable stocks and bonds	_____	_____	_____	_____
Cash, checking accounts, savings accounts, savings bonds, and money market investments	_____	_____	_____	_____
Notes, mortgages, and land contracts	_____	_____	_____	_____
Automobiles, boats, snowmobiles, and airplanes	_____	_____	_____	_____
Antiques, collections, art, jewelry	_____	_____	_____	_____
Other household furnishings	_____	_____	_____	_____
Other significant property	_____	_____	_____	_____
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____
Property held in revocable trusts (describe)	_____	_____	_____	_____
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____

**Wife**

	<u>Predeter- mination Date Property<sup>1</sup></u>	<u>Individual Property</u>	<u>Marital Property<sup>2</sup> (1/2 only)</u>	<u>Joint Tenancy and Survivorship Marital Property (1/2 only)</u>
Other interests in trusts (describe whether income or principal, mandatory or discretionary, termina- tion date(s), approximate value of trust assets)				
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____
_____	_____	_____	_____	_____
Secured debts other than mortgages deducted above (indicate security)				
_____	( )	( )	( )	( )
_____	( )	( )	( )	( )
Unsecured debts				
_____	( )	( )	( )	
_____	( )	( )	( )	
Death value of pension, profit- sharing, and other employ- ment benefits (Beneficiary _____)	_____	_____	_____	
Death value of HR-10 and IRA accounts (Beneficiary _____)	_____	_____	_____	

<u>Life insurance on life of wife</u>	<u>Face Amount</u>	<u>Current Cash Value<sup>4</sup></u>
1. Owned by wife <sup>3</sup> (Beneficiary _____)	\$ _____	\$ _____
2. Owned by husband (Beneficiary _____)	_____	_____
3. Owned by someone else (Beneficiary _____)	_____	_____

<u>Life insurance on life of another</u>	<u>Face Amount</u>	<u>Current Cash Value<sup>4</sup></u>	<u>Person Insured</u>
Owned by wife <sup>3</sup> (Beneficiary _____)	\$ _____	\$ _____	\$ _____

	Income		
	<u>Husband</u>	<u>Joint</u>	<u>Wife</u>
Last year's salary or other compensation	_____		_____
This year's estimated salary or other compensation	_____		_____
Other income last year	_____	_____	_____
Other estimated income this year	_____	_____	_____

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1. Consider the desirability of further subcategorizing predetermination date property into property that is deferred marital property and that which is not.

2. Mixed property should be treated as being entirely marital unless the nonmarital component can be traced, in which case the asset's value should be allocated between the marital property column and the other applicable columns.

3. *Owner* means the person appearing on the records of the policy issuer as the person having the ownership interest.

4. Net after any outstanding policy loans.

## **H. Sample Memorandum of Assets, Liabilities, and Income (Asset Disclosure by Title) [§ 7.170]**

### **1. Introduction [§ 7.171]**

The purpose of this Memorandum of Assets, Liabilities, and Income is to provide a framework for memorializing the parties' disclosures in a manner that will meet the fair and reasonable disclosure requirements of section 766.58(6)(c)1. It is a sample form only, and in some instances attachment of schedules listing one or more categories of assets or liabilities in greater detail may be appropriate.

### **2. Form [§ 7.172]**

#### **MEMORANDUM OF ASSETS, LIABILITIES, AND INCOME**

This memorandum has been prepared in connection with a marital property agreement to be executed by the undersigned on this date. Each party to that agreement and this memorandum certifies respectively that

1. He or she has made a fair and reasonable disclosure, reflected in this memorandum, of all assets, liabilities, and income in which he or she has any present or future vested or contingent interest, at approximate fair market values believed to be correct and accurate;

2. He or she understands that this memorandum categorizes the assets, liabilities, and income of each of the parties on the basis of title, possession, or who incurred the obligation (and not necessarily on the basis of ownership or liability for satisfaction), as they exist before the execution of the marital property agreement.

*[Choose appropriate alternative]*

3. He or she understands that before the execution of the marital property agreement, he or she may have had a marital property ownership interest in property listed in this memorandum that is titled in the name of, or possessed by, the other to the extent that all or part of such property was acquired after [1985] [the determination date] with income, with property traceable to income, or with other marital property. In addition, he or she understands that before the execution of the marital property agreement he or she may have had deferred marital

property elective rights under sections 861.02 to 861.06 of the Wisconsin Statutes in property titled in the name of, or possessed by, the other and that was acquired in whole or in part before [1986] [the determination date] with property that would have been marital property if the Wisconsin Marital Property Act had then been in effect.<sup>1</sup>

[Or]

3. Each party further understands that his or her marital property ownership interest may be reached by certain creditors even though he or she did not incur the obligation and is not personally liable for it.<sup>2</sup>

[Continue]

4. He or she further understands that the marital property agreement may change the ownership interests in assets or income, or the liabilities for obligations, as listed in this memorandum.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
(party's signature)

\_\_\_\_\_  
(party's signature)

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<sup>1</sup> Use with the opt-out agreement form in section 7.154, *supra*.

<sup>2</sup> Use with the opt-in agreement form in section 7.151, *supra*.

**Titled Assets and Liabilities**

	<u>Husband</u>	<u>Wife</u>	<u>Joint</u>
Principal residence (Less mortgage)	\$ ( )	\$ ( )	\$ ( )
Other residential property in Wisconsin (Less mortgage)	( )	( )	( )
Other residential property not in Wisconsin (Less mortgage)	( )	( )	( )
Investment real estate in Wisconsin (Less mortgage)	( )	( )	( )
Investment real estate not in Wisconsin (Less mortgage)	( )	( )	( )
Stock in closely held corporations	_____	_____	_____
Partnership interests	_____	_____	_____
Marketable stocks and bonds	_____	_____	_____
Checking accounts, savings accounts, savings bonds, and money market investments	_____	_____	_____
Notes, mortgages, and land contracts	_____	_____	_____
Automobiles, boats, snowmobiles, and airplanes	_____	_____	_____
Other significant property	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
Property held in revocable trusts (describe)	_____	_____	_____
Other interests in trusts (describe whether income or principal, mandatory or discretionary, termination date(s), approximate value of trust assets)	_____	_____	_____
Debts other than mortgages deducted above	( )	( )	( )
_____	( )	( )	( )

**Titled Assets and Liabilities**

	<u>Husband</u>	<u>Wife</u>	<u>Joint</u>
Death value of pension, profit-sharing, and other employment benefits (Husband's beneficiary _____ ) (Wife's beneficiary _____ )	_____	_____	
Death value of HR-10 and IRA accounts (Husband's beneficiary _____ ) (Wife's beneficiary _____ )	_____	_____	

	<u>Husband</u>	<u>Wife</u>
Life insurance on life of husband		
1. Owned by husband <sup>3</sup> (Beneficiary _____ ) (Face amount: \$ _____ ) Cash value <sup>4</sup> _____	\$ _____	
2. Owned by wife <sup>3</sup> (Beneficiary _____ ) (Face amount: \$ _____ ) Cash value <sup>4</sup> _____		\$ _____

Life insurance on life of wife		
1. Owned by wife <sup>3</sup> (Beneficiary _____ ) (Face amount: \$ _____ ) Cash value <sup>4</sup> _____		\$ _____
2. Owned by husband <sup>3</sup> (Beneficiary _____ ) (Face amount: \$ _____ ) Cash value <sup>4</sup> _____	\$ _____	

Life insurance on life of another		
1. Owned by husband <sup>3</sup> (Beneficiary _____ ) (Face amount: \$ _____ ) Cash value <sup>4</sup> _____	\$ _____	
2. Owned by wife <sup>3</sup> (Beneficiary _____ ) (Face amount: \$ _____ ) Cash value <sup>4</sup> _____		\$ _____



**Untitled Assets**

	<u>Husband</u>	<u>Wife</u>	<u>Joint</u>
Cash	_____	_____	_____
Jewelry	_____	_____	_____
Silver	_____	_____	_____
Furs	_____	_____	_____
Antiques	_____	_____	_____
Art	_____	_____	_____
Collections	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
Other household furnishings	_____	_____	_____
Other significant property	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____

**Income**

	<u>Husband</u>	<u>Wife</u>
Last year's salary or other compensation	_____	_____
This year's estimated salary or other compensation	_____	_____
Other income last year	_____	_____
Other estimated income this year	_____	_____

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3. Owner means a person appearing on the records of the policy issuer as the person having the ownership interest.

4. Net of any outstanding policy loans.

## **I. Sample Statutory Terminable Marital Property Classification Agreement (Including Termination and Financial Disclosure Forms) [§ 7.173]**

### **1. Introduction [§ 7.174]**

The wording of this agreement is taken directly from section 766.588. The spouses may execute only one such agreement without disclosure during their marriage. If provisions other than those contained in the statutory form are desired, the spouses must use a regular marital property agreement.

### **2. Form [§ 7.175]**

#### **NOTICE TO PERSONS WHO SIGN THIS AGREEMENT:**

1. A PROPERTY LAW KNOWN AS THE MARITAL PROPERTY SYSTEM GOVERNS THE PROPERTY RIGHTS OF MARRIED PERSONS IN WISCONSIN. AFTER THE MARITAL PROPERTY SYSTEM APPLIES TO A MARRIED COUPLE, EACH SPOUSE HAS AN UNDIVIDED ONE-HALF OWNERSHIP INTEREST IN PROPERTY, SUCH AS WAGES, DEFERRED EMPLOYMENT BENEFITS, LIFE INSURANCE, INCOME FROM PROPERTY AND CERTAIN APPRECIATION OF PROPERTY, THEREAFTER ACQUIRED DURING MARRIAGE DUE TO THE EFFORTS OF EITHER OR BOTH SPOUSES. PROPERTY WHICH IS BROUGHT TO THE MARRIAGE AND PROPERTY WHICH IS ACQUIRED BY ONE SPOUSE DURING THE MARRIAGE BY GIFT OR INHERITANCE IS NOT MARITAL PROPERTY BUT IS SOLELY OWNED BY THE ACQUIRING SPOUSE. THIS AGREEMENT ALTERS THE LAW GOVERNING YOUR PROPERTY RIGHTS. THE PURPOSE OF THE FOLLOWING INFORMATION IS TO APPRISE YOU, IN VERY GENERAL TERMS, OF SOME OF THE MORE IMPORTANT ASPECTS AND POSSIBLE EFFECTS OF THIS AGREEMENT. THE INFORMATION IS NOT INTENDED TO BE A PRECISE OR COMPLETE RECITATION OF THE LAW APPLICABLE TO THIS AGREEMENT AND IS NOT A SUBSTITUTE FOR LEGAL ADVICE.

2. BY ENTERING INTO THIS AGREEMENT, YOU HAVE AGREED TO RELINQUISH YOUR RIGHTS TO A SOLE OWNERSHIP INTEREST IN YOUR SOLELY OWNED PROPERTY; HOWEVER, YOU ARE ACQUIRING AUTOMATIC, EQUAL OWNERSHIP RIGHTS, WITH

YOUR SPOUSE, TO ALL PROPERTY THAT YOU AND YOUR SPOUSE OWN OR ACQUIRE.

3. THIS AGREEMENT MAY AFFECT:

A. YOUR ACCESS TO CREDIT AND THE PROPERTY AVAILABLE TO SATISFY OBLIGATIONS INCURRED BY YOU OR YOUR SPOUSE.

B. THE ACCUMULATION OF AND THE MANAGEMENT AND CONTROL OF PROPERTY BY YOU DURING YOUR MARRIAGE.

C. THE AMOUNT OF PROPERTY YOU HAVE TO DISPOSE OF AT YOUR DEATH.

D. YOUR TAXES.

E. ANY PREVIOUS MARRIAGE AGREEMENT ENTERED INTO BY YOU AND YOUR SPOUSE.

4. THIS AGREEMENT DOES NOT:

A. AFFECT RIGHTS AT DIVORCE.

B. ALTER THE LEGAL DUTY OF SUPPORT THAT SPOUSES HAVE TO EACH OTHER OR THAT A SPOUSE HAS TO HIS OR HER CHILDREN.

C. BY ITSELF PROVIDE THAT, UPON YOUR DEATH, YOUR MARITAL PROPERTY PASSES TO YOUR SURVIVING SPOUSE. IF THAT IS WHAT YOU INTEND, YOU ARE ENCOURAGED TO SEEK LEGAL ADVICE TO DETERMINE WHAT MUST BE DONE TO ACCOMPLISH THAT RESULT.

5. IN GENERAL, THIS AGREEMENT IS NOT BINDING ON CREDITORS UNLESS THE CREDITOR IS FURNISHED A COPY OF THE AGREEMENT BEFORE CREDIT IS EXTENDED. (It is not necessary to furnish a copy of the financial disclosure form.) IN ADDITION, THIRD PARTIES OTHER THAN CREDITORS MIGHT NOT BE BOUND BY THIS AGREEMENT UNLESS THEY HAVE ACTUAL KNOWLEDGE OF THE TERMS OF THE AGREEMENT.

6. IF YOU WISH TO AFFECT AN INTEREST IN YOUR REAL PROPERTY WITH THIS AGREEMENT, PARTICULARLY IN RELATION TO THIRD PARTIES, ADDITIONAL LEGAL PROCEDURES AND FORMALITIES MAY BE REQUIRED. IF YOU HAVE QUESTIONS

REGARDING THE EFFECT OF THIS AGREEMENT ON YOUR REAL PROPERTY, YOU ARE URGED TO SEEK LEGAL ADVICE.

7. IF YOU DO NOT COMPLETE SCHEDULE "A," "FINANCIAL DISCLOSURE," AND THE AGREEMENT BECOMES EFFECTIVE, THE AGREEMENT TERMINATES 3 YEARS AFTER THE DATE THAT YOU BOTH HAVE SIGNED THE AGREEMENT, AND YOU MAY NOT EXECUTE A SUBSEQUENT STATUTORY TERMINABLE MARITAL PROPERTY CLASSIFICATION AGREEMENT WITH THE SAME SPOUSE DURING THE SAME MARRIAGE UNLESS YOU COMPLETE THE FINANCIAL DISCLOSURE FORM. IF YOU INTEND THAT THIS AGREEMENT EXTEND BEYOND 3 YEARS, EACH OF YOU, BEFORE SIGNING THE AGREEMENT, MUST DISCLOSE TO THE OTHER YOUR EXISTING PROPERTY AND YOUR EXISTING FINANCIAL OBLIGATIONS, BY COMPLETING SCHEDULE "A," "FINANCIAL DISCLOSURE." IF SCHEDULE "A" HAS BEEN FILLED OUT BUT, IN A LEGAL ACTION AGAINST YOU TO ENFORCE THE AGREEMENT, YOU SHOW THAT THE INFORMATION ON SCHEDULE "A" DID NOT PROVIDE YOU WITH FAIR AND REASONABLE DISCLOSURE UNDER THE CIRCUMSTANCES, THE DURATION OF THE AGREEMENT IS 3 YEARS AFTER BOTH PARTIES SIGNED THE AGREEMENT.

8. ONE SPOUSE MAY TERMINATE THIS AGREEMENT AT ANY TIME BY GIVING SIGNED NOTICE OF TERMINATION TO THE OTHER SPOUSE. THE AGREEMENT TERMINATES 30 DAYS AFTER NOTICE IS GIVEN.

9. TERMINATION OF THIS AGREEMENT DOES NOT BY ITSELF CHANGE THE CLASSIFICATION OF PROPERTY CLASSIFIED BY THE AGREEMENT.

10. THIS AGREEMENT MAY BE AMENDED, REVOKED OR SUPPLEMENTED BY A LATER MARITAL PROPERTY AGREEMENT.

11. BOTH PARTIES MUST SIGN THIS AGREEMENT AND THE SIGNATURES MUST BE AUTHENTICATED BY OR ACKNOWLEDGED BEFORE A NOTARY. THE AGREEMENT BECOMES EFFECTIVE ON THE DATE THAT YOU HAVE BOTH SIGNED IT, THE DATE THAT YOU MARRY, OR THE DATE ON WHICH YOU ARE BOTH DOMICILED IN WISCONSIN, WHICHEVER IS LATER. IF YOU ALTER THE LANGUAGE OF THE AGREEMENT ON THIS FORM, THE AGREEMENT WILL NOT CONSTITUTE A STATUTORY TERMINABLE MARITAL PROPERTY CLASSIFICATION AGREEMENT (BUT IT MAY QUALIFY AS A GENERAL MARITAL PROPERTY AGREEMENT UNDER SECTION 766.58, WISCONSIN STATUTES).

12. EACH SPOUSE SHOULD RETAIN A COPY OF THIS AGREEMENT, INCLUDING ANY DISCLOSURE OF PROPERTY AND OBLIGATIONS, WHILE THE AGREEMENT IS IN EFFECT AND AFTER IT TERMINATES. RETENTION OF A COPY MAY BE IMPORTANT TO PROTECT INTERESTS ACQUIRED UNDER OR AFFECTED BY THE AGREEMENT.

13. IF AFTER ENTERING INTO THIS AGREEMENT ONE OR BOTH OF YOU ESTABLISH A DOMICILE OUTSIDE THIS STATE, YOU ARE URGED TO SEEK LEGAL ADVICE CONCERNING THE CONTINUED EFFECTIVENESS OF THIS AGREEMENT.

**STATUTORY TERMINABLE MARITAL PROPERTY  
CLASSIFICATION AGREEMENT  
(Pursuant to Section 766.588, Wisconsin Statutes)**

This agreement is entered into by \_\_\_\_\_ and \_\_\_\_\_ (husband and wife) (who intend to marry) (strike one). The parties hereby classify all of the property owned by them when this agreement becomes effective, and property acquired during the term of this agreement, as marital property.

One spouse may terminate this agreement at any time by giving signed notice of termination to the other spouse. Notice of termination by a spouse is given upon personal delivery or when sent by certified mail to the other spouse's last-known address. The agreement terminates 30 days after such notice is given.

The parties (have) (have not) (strike one) completed Schedule "A," "Financial Disclosure," attached to this agreement. If Schedule "A" has not been completed, the duration of this agreement is 3 years after both parties have signed the agreement. If Schedule "A" has been completed, the duration of this agreement is not limited to 3 years after it is signed.

IF THE DURATION OF THIS AGREEMENT IS NOT TO BE LIMITED TO 3 YEARS, MAKE SURE THAT SCHEDULE "A," "FINANCIAL DISCLOSURE," IS COMPLETED AND THAT YOU HAVE REVIEWED THE SCHEDULE BEFORE SIGNING THE AGREEMENT. IF YOU AND YOUR SPOUSE HAVE PREVIOUSLY ENTERED INTO A STATUTORY TERMINABLE MARITAL PROPERTY CLASSIFICATION AGREEMENT WITH EACH OTHER WHICH WAS EFFECTIVE DURING YOUR PRESENT MARRIAGE, AND YOU AND YOUR SPOUSE DID NOT COMPLETE SCHEDULE "A," YOU MAY NOT EXECUTE THIS AGREEMENT IF YOU DO NOT COMPLETE SCHEDULE "A."

Signature of One Spouse: \_\_\_\_\_

Date: \_\_\_\_\_

Print Name Here: \_\_\_\_\_

Residence Address: \_\_\_\_\_

(Make Sure Your Signature is Authenticated  
or Acknowledged Below.)

**AUTHENTICATION**

Signature \_\_\_\_\_ authenticated this \_\_\_\_\_ day of  
\_\_\_\_\_, (year)

\* \_\_\_\_\_



STATE OF WISCONSIN )  
 ) ss.  
\_\_\_\_\_ County )

Personally came before me this \_\_\_\_\_ day of \_\_\_\_\_, (year)  
the above named \_\_\_\_\_ to me known to be the person who  
executed the foregoing instrument and acknowledge the same.

\* \_\_\_\_\_  
Notary Public \_\_\_\_\_, \_\_\_\_\_ County, Wisconsin.  
My Commission is permanent.  
(If not, state expiration date: \_\_\_\_\_, (year))

(Signatures may be authenticated or acknowledged. Both are not necessary.)

\*Names of persons signing in any capacity should be typed or printed below their signatures.

**TERMINATION OF STATUTORY TERMINABLE  
MARITAL PROPERTY CLASSIFICATION AGREEMENT**

I UNDERSTAND THAT:

1. THIS TERMINATION TAKES EFFECT 30 DAYS AFTER MY SPOUSE IS NOTIFIED OF THE TERMINATION, AS PROVIDED UNDER SECTION 766.588(4) OF THE WISCONSIN STATUTES.

2. THIS TERMINATION IS PROSPECTIVE; IT DOES NOT AFFECT THE CLASSIFICATION OF PROPERTY ACQUIRED BEFORE THE TERMINATION BECOMES EFFECTIVE. PROPERTY ACQUIRED AFTER THE TERMINATION BECOMES EFFECTIVE IS CLASSIFIED AS PROVIDED UNDER THE MARITAL PROPERTY LAW.

3. IN GENERAL, THIS TERMINATION IS NOT BINDING ON CREDITORS UNLESS THEY ARE PROVIDED A COPY OF THE TERMINATION BEFORE CREDIT IS EXTENDED.

The undersigned terminates the statutory terminable marital property classification agreement entered into by me and my spouse on \_\_\_\_\_ (date last spouse signed the agreement) under section 766.588 of the Wisconsin Statutes.



Signature: \_\_\_\_\_  
Date: \_\_\_\_\_  
Print Name Here: \_\_\_\_\_  
Residence Address: \_\_\_\_\_

### **SCHEDULE "A" FINANCIAL DISCLOSURE**

The following general categories of assets and liabilities are not all-inclusive, and if other assets or liabilities exist, they should be listed. Assets should be listed according to which spouse has title (including assets owned by a spouse or the spouses with one or more third parties) and at their approximate market value.

**SCHEDULE "A"**  
**FINANCIAL DISCLOSURE**

The following general categories of assets and liabilities are not all-inclusive, and if other assets or liabilities exist, they should be listed. Assets should be listed according to which spouse has title (including assets owned by a spouse or the spouses with one or more third parties) and at their approximate market value.

	<u>Husband</u>	<u>Wife</u>	<u>Both Names</u>
I. ASSETS:			
A. Real Estate (gross value)			
B. Stocks, bonds and mutual funds			
C. Accounts at and certificates or other instruments issued by financial institutions			
D. Mortgages, land contracts, promissory notes and cash			
E. Partnership interests			
F. Trust interests			
G. Livestock, farm products, crops			
H. Automobiles and other vehicles			
I. Jewelry and personal effects			
J. Household furnishings			
K. Life insurance and annuities:			
1. Face value			
2. Cash surrender value			
L. Retirement benefits (include value):			
1. Pension plans			
2. Profit-sharing plans			
3. HR-10 KEOGH plans			
4. IRAs			
5. Deferred compensation plans			
M. Other assets not listed elsewhere			
II. OBLIGATIONS (TOTAL OUTSTANDING BALANCE):			
A. Mortgages and liens			
B. Credit cards			
C. Other obligations to financial institutions			
D. Alimony, maintenance, and child support (per month)			
E. Other obligations (such as other obligations to individuals, guarantees, contingent liabilities)			

	<u>Husband</u>	<u>Wife</u>	<u>Both Names</u>
III. ANNUAL COMPENSATION FOR SERVICES: (for example, wages and income from self-employment; also include social security, disability and similar income here)	_____	_____	_____

(IF YOU NEED ADDITIONAL SPACE, ADD ADDITIONAL SHEETS)

## **J. Sample Statutory Terminable Individual Property Classification Agreement (Including Termination and Financial Disclosure Forms) [§ 7.176]**

### **1. Introduction [§ 7.177]**

The wording of this agreement is taken directly from section 766.589. The spouses may execute only one such agreement without disclosure during their marriage. If provisions other than those contained in the statutory form are desired, the spouses must use a regular marital property agreement.

### **2. Form [§ 7.178]**

#### **NOTICE TO PERSONS WHO SIGN THIS AGREEMENT:**

1. A PROPERTY LAW KNOWN AS THE MARITAL PROPERTY SYSTEM GOVERNS THE PROPERTY RIGHTS OF MARRIED PERSONS IN WISCONSIN. AFTER THE MARITAL PROPERTY SYSTEM APPLIES TO A MARRIED COUPLE, EACH SPOUSE HAS AN UNDIVIDED ONE-HALF OWNERSHIP INTEREST IN PROPERTY, SUCH AS WAGES, DEFERRED EMPLOYMENT BENEFITS, LIFE INSURANCE, INCOME FROM PROPERTY AND CERTAIN APPRECIATION OF PROPERTY, THEREAFTER ACQUIRED DURING MARRIAGE DUE TO THE EFFORTS OF EITHER OR BOTH SPOUSES. THIS AGREEMENT ALTERS THE LAW GOVERNING YOUR PROPERTY RIGHTS. THE PURPOSE OF THE FOLLOWING INFORMATION IS TO APPRISE YOU, IN VERY GENERAL TERMS, OF SOME OF THE MORE IMPORTANT ASPECTS AND POSSIBLE EFFECTS OF THIS AGREEMENT. THE INFORMATION IS NOT INTENDED TO BE A PRECISE OR COMPLETE RECITATION OF THE LAW APPLICABLE TO THIS AGREEMENT AND IS NOT A SUBSTITUTE FOR LEGAL ADVICE.

2. BY ENTERING INTO THIS AGREEMENT, YOU HAVE AGREED TO RELINQUISH YOUR RIGHTS TO AN AUTOMATIC OWNERSHIP INTEREST IN PROPERTY ACQUIRED AS A RESULT OF SPOUSAL EFFORT DURING MARRIAGE AND THE TERM OF THE AGREEMENT; HOWEVER, YOU ARE ACQUIRING AUTOMATIC OWNERSHIP RIGHTS TO PROPERTY TITLED IN YOUR NAME.

3. THIS AGREEMENT MAY AFFECT:

A. YOUR ACCESS TO CREDIT AND THE PROPERTY AVAILABLE TO SATISFY OBLIGATIONS INCURRED BY YOU OR YOUR SPOUSE.

B. THE ACCUMULATION OF AND THE MANAGEMENT AND CONTROL OF PROPERTY BY YOU DURING YOUR MARRIAGE.

C. THE AMOUNT OF PROPERTY YOU HAVE TO DISPOSE OF AT YOUR DEATH.

D. YOUR TAXES.

E. ANY PREVIOUS MARRIAGE AGREEMENT ENTERED INTO BY YOU AND YOUR SPOUSE.

4. THIS AGREEMENT DOES NOT:

A. AFFECT RIGHTS AT DIVORCE.

B. ALTER THE LEGAL DUTY OF SUPPORT THAT SPOUSES HAVE TO EACH OTHER OR THAT A SPOUSE HAS TO HIS OR HER CHILDREN.

5. NOTWITHSTANDING THIS AGREEMENT, THE PROPERTY CLASSIFIED BY THIS AGREEMENT THAT IS OWNED BY THE FIRST SPOUSE TO DIE IS SUBJECT TO CERTAIN ELECTIVE RIGHTS OF THE SURVIVING SPOUSE. YOU MAY BAR THESE ELECTIVE RIGHTS BY SEPARATE MARITAL PROPERTY AGREEMENT.

6. IN GENERAL, THIS AGREEMENT IS NOT BINDING ON CREDITORS UNLESS THE CREDITOR IS FURNISHED A COPY OF THE AGREEMENT BEFORE CREDIT IS EXTENDED. (IT IS NOT NECESSARY TO FURNISH A COPY OF THE FINANCIAL DISCLOSURE FORM.) IN ADDITION, THIRD PARTIES OTHER THAN CREDITORS MIGHT NOT BE BOUND BY THIS AGREEMENT UNLESS THEY HAVE ACTUAL KNOWLEDGE OF THE TERMS OF THE AGREEMENT.

7. IF YOU WISH TO AFFECT AN INTEREST IN YOUR REAL PROPERTY WITH THIS AGREEMENT, PARTICULARLY IN RELATION TO THIRD PARTIES, ADDITIONAL LEGAL PROCEDURES AND FORMALITIES MAY BE REQUIRED. IF YOU HAVE QUESTIONS REGARDING THE EFFECT OF THIS AGREEMENT ON YOUR REAL PROPERTY, YOU ARE URGED TO SEEK LEGAL ADVICE.

8. IF YOU DO NOT COMPLETE SCHEDULE "A," "FINANCIAL DISCLOSURE," AND THE AGREEMENT BECOMES EFFECTIVE, THE AGREEMENT TERMINATES 3 YEARS AFTER THE DATE THAT YOU BOTH HAVE SIGNED THE AGREEMENT, AND YOU MAY NOT EXECUTE A SUBSEQUENT STATUTORY TERMINABLE INDIVIDUAL PROPERTY CLASSIFICATION AGREEMENT WITH THE SAME SPOUSE DURING THE SAME MARRIAGE UNLESS YOU COMPLETE THE FINANCIAL DISCLOSURE FORM. IF YOU INTEND THAT THIS AGREEMENT EXTEND BEYOND 3 YEARS, EACH OF YOU, BEFORE SIGNING THE AGREEMENT, MUST DISCLOSE TO THE OTHER YOUR EXISTING PROPERTY AND YOUR EXISTING FINANCIAL OBLIGATIONS, BY COMPLETING SCHEDULE "A," "FINANCIAL DISCLOSURE." IF SCHEDULE "A" HAS BEEN FILLED OUT BUT IN A LEGAL ACTION AGAINST YOU TO ENFORCE THE AGREEMENT YOU SHOW THAT THE INFORMATION ON SCHEDULE "A" DID NOT PROVIDE YOU WITH FAIR AND REASONABLE DISCLOSURE UNDER THE CIRCUMSTANCES, THE DURATION OF THE AGREEMENT IS 3 YEARS AFTER BOTH PARTIES SIGNED THE AGREEMENT.

9. ONE SPOUSE MAY TERMINATE THIS AGREEMENT AT ANY TIME BY GIVING SIGNED NOTICE OF TERMINATION TO THE OTHER SPOUSE. THE AGREEMENT TERMINATES 30 DAYS AFTER NOTICE IS GIVEN. IF SUCH NOTICE OF TERMINATION IS GIVEN BY ONE SPOUSE TO THE OTHER SPOUSE, EACH SPOUSE HAS A DUTY TO THE OTHER SPOUSE TO ACT IN GOOD FAITH IN MATTERS INVOLVING THE PROPERTY OF THE SPOUSE WHO IS REQUIRED TO ACT IN GOOD FAITH THAT HAS BEEN CLASSIFIED AS INDIVIDUAL PROPERTY BY THIS AGREEMENT. THE GOOD FAITH DUTY CONTINUES UNTIL THE AGREEMENT TERMINATES (30 DAYS AFTER NOTICE IS GIVEN).

10. TERMINATION OF THIS AGREEMENT DOES NOT BY ITSELF CHANGE THE CLASSIFICATION OF PROPERTY CLASSIFIED BY THE AGREEMENT.

11. THIS AGREEMENT MAY BE AMENDED, REVOKED OR SUPPLEMENTED BY A LATER MARITAL PROPERTY AGREEMENT.

12. BOTH PARTIES MUST SIGN THIS AGREEMENT, AND THE SIGNATURES MUST BE AUTHENTICATED OR ACKNOWLEDGED BEFORE A NOTARY. THE AGREEMENT BECOMES EFFECTIVE ON THE DATE THAT YOU HAVE BOTH SIGNED IT, THE DATE THAT YOU MARRY, OR THE DATE ON WHICH YOU ARE BOTH DOMICILED IN WISCONSIN, WHICHEVER IS LATER. IF YOU ALTER THE LANGUAGE OF THE AGREEMENT ON THIS FORM, THE AGREEMENT WILL NOT CONSTITUTE A STATUTORY TERMINABLE

INDIVIDUAL PROPERTY CLASSIFICATION AGREEMENT (BUT IT MAY QUALIFY AS A GENERAL MARITAL PROPERTY AGREEMENT UNDER SECTION 766.58, WISCONSIN STATUTES).

13. EACH SPOUSE SHOULD RETAIN A COPY OF THIS AGREEMENT, INCLUDING ANY DISCLOSURE OF PROPERTY AND OBLIGATIONS, WHILE THE AGREEMENT IS IN EFFECT AND AFTER IT TERMINATES. RETENTION OF A COPY MAY BE IMPORTANT TO PROTECT INTERESTS ACQUIRED UNDER OR AFFECTED BY THE AGREEMENT.

14. IF AFTER ENTERING INTO THIS AGREEMENT ONE OR BOTH OF YOU ESTABLISH A DOMICILE OUTSIDE THIS STATE, YOU ARE URGED TO SEEK LEGAL ADVICE CONCERNING THE CONTINUED EFFECTIVENESS OF THIS AGREEMENT.

**STATUTORY TERMINABLE INDIVIDUAL PROPERTY  
CLASSIFICATION AGREEMENT  
(Pursuant to Section 766.589, Wisconsin Statutes)**

This agreement is entered into by \_\_\_\_\_ and \_\_\_\_\_ (husband and wife) (who intend to marry) (strike one). The parties hereby classify the marital property owned by them when this agreement becomes effective, and property acquired during the term of this agreement that would otherwise have been marital property, as the individual property of the owning spouse. The parties agree that ownership of such property shall be determined by the name in which the property is held and, if property is not held by either or both spouses, ownership shall be determined as if the parties were unmarried persons when the property was acquired.

Upon the death of either spouse, the surviving spouse may, except as otherwise provided in a subsequent marital property agreement, and regardless of whether this agreement has terminated, elect against the property of the decedent spouse as provided in section 766.589(7) of the Wisconsin Statutes.

One spouse may terminate this agreement at any time by giving signed notice of termination to the other spouse. Notice of termination by a spouse is given upon personal delivery or when sent by certified mail to the other spouse's last-known address. The agreement terminates 30 days after such notice is given.

The parties (have) (have not) (strike one) completed Schedule "A," "Financial Disclosure," attached to this agreement. If Schedule "A" has

not been completed, the duration of this agreement is 3 years after both parties have signed the agreement. If Schedule "A" has been completed, the duration of this agreement is not limited to 3 years after it is signed.

IF THE DURATION OF THIS AGREEMENT IS NOT TO BE LIMITED TO 3 YEARS, MAKE SURE THAT SCHEDULE "A," "FINANCIAL DISCLOSURE," IS COMPLETED AND THAT YOU HAVE REVIEWED THE SCHEDULE BEFORE SIGNING THE AGREEMENT. IF YOU AND YOUR SPOUSE HAVE PREVIOUSLY ENTERED INTO A STATUTORY TERMINABLE INDIVIDUAL PROPERTY CLASSIFICATION AGREEMENT WITH EACH OTHER WHICH WAS EFFECTIVE DURING YOUR PRESENT MARRIAGE, AND YOU AND YOUR SPOUSE DID NOT COMPLETE SCHEDULE "A," YOU MAY NOT EXECUTE THIS AGREEMENT IF YOU DO NOT COMPLETE SCHEDULE "A."



Signature of One Spouse: \_\_\_\_\_  
Date: \_\_\_\_\_  
Print Name Here: \_\_\_\_\_  
Residence Address: \_\_\_\_\_

(Make Sure Your Signature is Authenticated  
or Acknowledged Below.)

**AUTHENTICATION**

Signature \_\_\_\_\_ authenticated this \_\_\_\_\_ day of  
\_\_\_\_\_, (year)

\*

TITLE: MEMBER STATE BAR OF WISCONSIN  
(If not, .... authorized by s. 706.06, Wis. Stats.)

**ACKNOWLEDGMENT**

STATE OF WISCONSIN )  
                                  ) ss.  
County )

Personally came before me this \_\_\_\_\_ day of \_\_\_\_\_, (year)  
the above named \_\_\_\_\_ to me known to be the person  
who executed the foregoing instrument and acknowledge the same.

\*

Notary Public \_\_\_\_\_, \_\_\_\_\_ County, Wisconsin.  
My Commission is permanent.  
(If not, state expiration date: \_\_\_\_\_, (year))

(Signatures may be authenticated or acknowledged. Both are not necessary.)

\*Names of persons signing in any capacity should be typed or printed  
below their signatures.

Signature of Other Spouse: \_\_\_\_\_  
Date: \_\_\_\_\_  
Print Name Here: \_\_\_\_\_  
Residence Address: \_\_\_\_\_

## AUTHENTICATION

★ \_\_\_\_\_

## ACKNOWLEDGMENT

★ \_\_\_\_\_

\*Names of persons signing in any capacity should be typed or printed below their signatures.

I UNDERSTAND THAT:

2. THIS TERMINATION IS PROSPECTIVE; IT DOES NOT AFFECT THE CLASSIFICATION OF PROPERTY ACQUIRED BEFORE THE TERMINATION BECOMES EFFECTIVE. PROPERTY ACQUIRED

AFTER THE TERMINATION BECOMES EFFECTIVE IS CLASSIFIED AS PROVIDED UNDER THE MARITAL PROPERTY LAW.

3. IN GENERAL, THIS TERMINATION IS NOT BINDING ON CREDITORS UNLESS THEY ARE PROVIDED A COPY OF THE TERMINATION BEFORE CREDIT IS EXTENDED.

The undersigned terminates the statutory terminable individual property classification agreement entered into by me and my spouse on \_\_\_\_\_ (date last spouse signed the agreement) under section 766.589 of the Wisconsin Statutes.

Signature: \_\_\_\_\_

Date: \_\_\_\_\_

Print Name Here: \_\_\_\_\_

Residence Address: \_\_\_\_\_

#### **SCHEDULE "A" FINANCIAL DISCLOSURE**

The following general categories of assets and liabilities are not all inclusive, and if other assets or liabilities exist, they should be listed. Assets should be listed according to which spouse has title (including assets owned by a spouse or the spouses with one or more third parties) and at their approximate market value.

	<u>Husband</u>	<u>Wife</u>	<u>Both Names</u>
I. ASSETS:			
A. Real Estate (gross value)	_____	_____	_____
B. Stocks, bonds and mutual funds	_____	_____	_____
C. Accounts at and certificates or other instruments issued by financial institutions	_____	_____	_____
D. Mortgages, land contracts, promissory notes and cash	_____	_____	_____
E. Partnership interests	_____	_____	_____
F. Trust interests	_____	_____	_____
G. Livestock, farm products, crops	_____	_____	_____
H. Automobiles and other vehicles	_____	_____	_____
I. Jewelry and personal effects	_____	_____	_____
J. Household furnishings	_____	_____	_____
K. Life insurance and annuities:			
1. Face value	_____	_____	_____
2. Cash surrender value	_____	_____	_____
L. Retirement benefits (include value):			
1. Pension plans	_____	_____	_____
2. Profit-sharing plans	_____	_____	_____
3. HR-10 KEOGH plans	_____	_____	_____
4. IRAs	_____	_____	_____
5. Deferred compensation plans	_____	_____	_____
M. Other assets not listed elsewhere	_____	_____	_____
II. OBLIGATIONS (TOTAL OUTSTANDING BALANCE):			
A. Mortgages and liens	_____	_____	_____
B. Credit cards	_____	_____	_____
C. Other obligations to financial institutions	_____	_____	_____
D. Alimony, maintenance, and child support (per month)	_____	_____	_____
E. Other obligations (such as other obligations to individuals, guarantees, contingent liabilities)	_____	_____	_____
III. ANNUAL COMPENSATION FOR SERVICES: (for example, wages and income from self-employment; also include social security, disability and similar income here)	_____	_____	_____

(IF YOU NEED ADDITIONAL SPACE, ADD ADDITIONAL SHEETS)

## Interspousal and Other Remedies

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## I. Scope of Chapter [§ 8.1]

Just as the Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or the Wisconsin Marital Property Act], created new ownership rights, it also created new causes of action between spouses during an ongoing marriage and new causes of action by a spouse against a third party to whom the other spouse has transferred marital property. The remedies provided are consistent with

the rights of ownership created by the Act. Inherent in the concept of ownership is the right to seek redress if one's property rights have been violated and damage results. This chapter examines the duties that spouses owe to each other and the causes of action that may result if these duties are breached.<sup>1</sup>

## **II. Duties of Spouses with Respect to Personal Obligations and Property [§ 8.2]**

### **A. Duty of Support [§ 8.3]**

#### **1. Personal Obligation of One Spouse to the Other for Support [§ 8.4]**

The duty of one spouse to the other for support is a personal obligation. Each spouse has an equal obligation to support the other spouse and his or her minor children. Wis. Stat. § 765.001(2). This equal obligation means that neither spouse is presumed to have the primary obligation for support. *Id.* Although the obligation is equal, each spouse's individual obligation is measured on a case-by-case basis "in accordance with his or her ability to contribute money or services or both which are necessary for the adequate support and maintenance of his or her minor children and of the other spouse." *Id.*; *see supra* § 5.31; *infra* ch. 11.

Failure to fulfill this duty results in creation of a potential cause of action by one spouse against the other under section 767.501. *See infra* § 8.17. Section 767.501 was not created by the Act. The action under section 767.501 is among those involving the family that are enumerated in section 767.001 and the procedural rules of chapter 767 apply. The level of the support obligation is determined according to the considerations enumerated in section 767.511, which deals with child support, and section 767.56, which deals with maintenance. Wis. Stat.

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<sup>1</sup> Unless otherwise indicated, all references to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189, and all references to the United States Code (U.S.C.) are current through Pub. L. No. 111-133 (Mar. 2, 2010). Textual references to the Wisconsin Statutes are hereinafter indicated as "chapter xxx" or "section xxx.xx," without the designation "of the Wisconsin Statutes."



§ 767.501(2)(b). In some cases, unjustified failure to support may also result in criminal sanctions. *See* Wis. Stat. § 948.22; *State v. Grayson*, 172 Wis. 2d 156, 493 N.W.2d 23 (1992); *State v. Monarch*, 230 Wis. 2d 542, 602 N.W.2d 179 (Ct. App. 1999); *State v. Duprey*, 149 Wis. 2d 655, 439 N.W.2d 837 (Ct. App. 1989). An additional means of fulfilling the obligation of support is created by section 766.55(2)(a). A spouse may bring an action against the other spouse who has a support obligation. This obligation may be satisfied from all marital property and from all other property of the “obligated” spouse. The amount of support payments ordered would probably be the same in actions brought under sections 767.501 and 766.55(2)(a).

Each spouse’s obligation to the other continues notwithstanding the incompetency of the obligated spouse, and a guardian of the estate has the continuing duty to expend assets of the estate for the ward and his or her dependents, including a spouse. Wis. Stat. § 54.19(4).

## **2. Liability of Spouses to Creditors [§ 8.5]**

The obligated spouse might not be the spouse who incurs obligations during the course of providing support for the family because the extent of each spouse’s financial obligation under section 765.001(2) might not be equal. The nonincurring spouse may be better able to provide financial support than the incurring spouse, thereby making the nonincurring spouse the one personally obligated. *Id.* An action by a creditor to enforce a support obligation incurred by a spouse may be appropriate when the incurring spouse does not have access to sufficient funds to pay creditors who have extended credit for goods and services required for the support of the spouses and minor children. Each spouse is personally obligated to the creditor to the extent that he or she has property to satisfy the obligation. *St. Marys Hosp. Med. Ctr. v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 706 (Ct. App. 1994). This personal obligation continues even though the spouses are divorced after the obligation is incurred. *Id.* An obligation arising under the doctrine of necessities is categorized as a support obligation under section 766.55(2)(a), thus making all assets classified as marital property and all other property of both spouses subject to recovery. *Id.*; *see infra* § 8.6.

### 3. Necessaries Doctrine [§ 8.6]

The common law doctrine of necessities also creates a direct, personal liability from the obligated spouse to the creditor who has provided goods and services necessary for the support of the recipient spouse and minor children, even if the obligated spouse has not dealt directly with the creditor. *St. Marys Hosp. Med. Ctr.*, 186 Wis. 2d 100. Obligations falling under the necessities doctrine are support obligations under section 766.55(2)(a). Consequently, the obligated, nonincurring spouse's nonmarital property is available to satisfy the obligation. The burden of pursuing the obligated spouse for payment is therefore borne by the creditor rather than by the recipient spouse.

The necessities doctrine is intended to facilitate the delivery of necessary goods and services because a creditor is more likely to deal directly with a nonemployed spouse if the creditor knows that the employed spouse is also legally obligated to the creditor. Moreover, the nonemployed spouse is able to receive such goods and services without resorting to court action against his or her spouse.

Before the Act, the husband was primarily liable and the wife secondarily liable for necessities. *See Marshfield Clinic v. Discher*, 105 Wis. 2d 506, 314 N.W.2d 326 (1982); *Stromsted v. St. Michael Hosp. of Franciscan Sisters (In re Estate of Stromsted)*, 99 Wis. 2d 136, 299 N.W.2d 226 (1980); *Sharpe Furniture, Inc. v. Buckstaff*, 99 Wis. 2d 114, 299 N.W.2d 219 (1980). This priority of liability was intended to reflect the economic disparity between men and women. Section 765.001(2) equalizes the support obligations of spouses even though on a case-by-case basis one spouse may be found to have a greater financial obligation. Under the Act, neither the husband nor the wife is presumed to be primarily liable to a creditor under the doctrine of necessities. Wis. Stat. § 765.001(2); *St. Marys Hosp. Med. Ctr.*, 186 Wis. 2d 100. To the extent that the marital property system equalizes ownership of property between spouses, the need for this priority is diminished.

## **B. Duties of Spouses Pending Termination of the Marriage [§ 8.7]**

### **1. Transfers in Contemplation of Divorce [§ 8.8]**

Before January 1, 1986, the effective date of the Act, spouses in Wisconsin were essentially free to manage their property as they chose as long as they fulfilled their obligations of support. Actions taken in contemplation of divorce, however, were subject to scrutiny by the court and were considered in determining a spouse's rights in property at divorce. For example, under section 767.63 (formerly section 767.275), which was not changed by the Act, any asset valued at \$500 or more that was transferred for inadequate consideration, wasted, given away, or otherwise unaccounted for within one year of the commencement of the action, and that would have been part of the estate but for the actions of the spouse disposing of the asset, is considered part of the estate in determining the property division under section 767.61. Wis. Stat. § 767.63; *see also* Wis. Stat. § 767.117(1)(b) (prohibiting spouses after filing of petition for dissolution from encumbering, concealing, damaging, destroying, transferring, or otherwise disposing of spouses' property except under certain circumstances).

The statutory provision relating to one spouse's intentionally disposing of assets before divorce to deprive the other spouse of his or her share is not the only protection in Wisconsin for spouses contemplating divorce. The Wisconsin courts have at the time of divorce protected one spouse from the wasteful propensities of the other, whether or not the wrongful disposition of assets was done in contemplation of the dissolution of the marriage. In *Anstutz v. Anstutz*, 112 Wis. 2d 10, 331 N.W.2d 844 (Ct. App. 1983), the court held that an innocent spouse may receive a larger share of the estate than the spouse who has depleted the estate through squandering and neglect. The court's rationale in *Anstutz* was that the contributions to the marriage may be offset by negative factors resulting in loss of the marital estate. *Id.* at 12–13. Such factors should be considered when determining total contributions to the marriage under section 767.61(3)(d).

Similarly, after the Act became effective, the court of appeals held in *Gardner v. Gardner*, 175 Wis. 2d 420, 499 N.W.2d 266 (Ct. App. 1993), that section 767.255 (now section 767.61) provides the exclusive means in a dissolution action to compensate a spouse allegedly defrauded of his

or her interest in marital property assets by the other spouse's intentional misrepresentation. Citing *Anstutz*, the court held that remedies under section 766.70 and the common law tort of misrepresentation are unavailable after a dissolution action is commenced. 175 Wis. 2d at 427–31. Moreover, these statutory remedies are unnecessary because comprehensive remedies are available under sections 767.255 and .275 (now sections 767.61 and .63). *See infra* §§ 8.18, .61; *see also Terry v. Terry*, 565 So. 2d 997, 1001–02 (La. Ct. App. 1990) (holding, under Louisiana law, that spouse managing community property asset has fiduciary duty to other spouse until community is partitioned after dissolution; duty extends to management of corporations, stock of which is community property, by spouses); Laura Breisky, *The Duty of Disclosure Between Spouses Dividing a Common Business Interest*, 2 Community Prop. Alert 1 (No. 4, July 1990).

While intentional harm to the other spouse's economic interests might affect property division, unintentional harm might not. The court in *Hauge v. Hauge*, 145 Wis. 2d 600, 427 N.W.2d 154 (Ct. App. 1988), did not find that the loss of divisible assets because of the husband's poor investment decisions was sufficient to overcome the presumption of equal division. The husband had used poor judgment in his exercise of management and control over assets that would have been subject to division. Nonetheless, he had intended to make a profit, and the fact that he had management and control did not warrant the court giving the wife a greater share in the property division.

Other community property states impose a general duty to account for community property before dissolution of the marriage. This right does not exist in those states during the ongoing marriage. *See supra* ch. 4. If the spouse's explanation of the disposition of the assets is unsatisfactory, the other spouse may be compensated in the dissolution action for the loss. For example, Louisiana requires that a spouse account for "community property under his control at the termination of the community property regime." La. Civ. Code Ann. art. 2369 (WESTLAW current through the 2009 Regular Session); *see also Jackson v. Jackson*, 425 So. 2d 379, 383 (La. Ct. App. 1982) (requiring husband to account for community property savings account in his name, from which he had withdrawn entire amount shortly before parties' separation). Other community property states without such statutes impose a similar duty by case law. *See* William A. Reppy, Jr. & Cynthia A. Samuel, *Community Property in the United States* 245–49 (2d ed. 1982). *See also* the discussion of cases involving the duty to account for

community property in a spouse's possession before dissolution of marriage in chapter 4, *supra*.

The Act allows the protections provided by section 767.63 and cases like *Anstutz* to continue. In addition, the Act permits one spouse to obtain an accounting of the spouses' property from the other spouse under section 766.70(2). *See infra* § 8.20.

## **2. Transfers in Fraud of Rights of Surviving Spouse [§ 8.9]**

In general, if a spouse has transferred property or made arrangements for the transfer of property with the primary purpose of defrauding the rights of the surviving spouse in such property, the surviving spouse may be able to recover the property from the recipient. Wis. Stat. § 861.17. The surviving spouse may be able to recover either the share that he or she would have otherwise received under chapter 861 (Family Rights) or chapter 852 (Intestate Succession), or the surviving spouse's interest in marital property. Wis. Stat. § 861.17(3), (3m); *see also infra* §§ 8.18, .44–.59 (remedies under the Act for transfers of marital property).

## **C. Good-faith Duty Under the Act [§ 8.10]**

### **1. In General [§ 8.11]**

Before the Act became effective, spouses in Wisconsin owed each other an economic duty for support during the marriage and a duty to refrain from taking actions with the intent to deprive the other spouse of property rights at the termination of the marriage. *See supra* §§ 8.3–.9. In other respects, each spouse generally could manage his or her property free of any claim by or duty to the other spouse.

The Act, however, created a duty of good faith related to the management of marital property and the nonmarital property of the other spouse. Wis. Stat. § 766.15; *see supra* ch. 4. The nature of marital property makes such a duty necessary; that is, the spouse who solely holds marital property has sole management and control over that property, even though it is owned equally by both spouses. *See* Wis. Stat. § 766.51(1)(am). To protect the property interests of the

nonmanaging spouse, the Act requires that the managing spouse act in good faith with respect to the other spouse's property. Wis. Stat. § 766.15. In contrast to the limited pre-Act duties that one spouse owed the other—namely, the duty of support and the duty of refraining from certain property transfers, the duty of good faith is an attempt to protect the property interests of both spouses *during* the ongoing marriage as well as at the termination of the marriage by death or dissolution.

A Wisconsin case addressed a spouse's duties with respect to the management of the spouse's individual and marital property in the context of a property division at the dissolution of the marriage. In *Noble v. Noble*, 2005 WI App 227, 287 Wis. 2d 699, 706 N.W.2d 166, the wife asked the court of appeals to increase the amount of property awarded to her because of the alleged waste of marital assets.

Danny and Dale Noble were brothers in the partnership that originally included their father. It is not clear from the decision, but it appears that at least a portion of the partnership may have been Danny's individual property at the time of his divorce from Deborah, while the remaining portion was marital property subject to division. The partnership owned no real estate; this was owned either by the brothers, or in the case of real estate that Danny's wife, Deborah, asserted should have been included in property to be divided, by Dale and his wife. All the real estate was used in the farming operation, but later-acquired real estate was put in the name of Dale and his wife, giving Danny no interest. All parties admitted the real estate was acquired in this manner to prevent Deborah from acquiring an interest if she and Danny divorced.

The court held that the marital estate was not diminished or wasted by Danny's failure to obtain an interest in the real estate. As to the use of the marital asset in which he had an interest, the court found that the repayment structure enabled Deborah to obtain her proper share in the property division. Dale and his wife borrowed from the partnership the money to purchase the real estate, and the partnership paid rent at market value in the form of forgiveness of that debt. The remaining receivable was included in the value of the partnership at the time of the dissolution and became part of the property division. The court distinguished waste, which assumes that assets are no longer in the estate, from the failure to take advantage of an opportunity to increase the marital estate.

In short, the law does not require a party to a prospective divorce to take advantage of an opportunity to acquire property that would increase the

value of the marital estate, and the use of partnership funds to finance the purchase of the properties did not improperly dissipate the value of the marital estate.

*Id.* ¶ 2; see Matthew J. Price, *Case Spotlight: Noble v. Noble*, 26 Wis. J. Fam. L. 24 (2006); see also *Somps v. Somps*, 58 Cal. Rptr. 304 (Ct. App. 1967) (holding that husband did not breach good-faith duty by taking advantage of investment opportunity for separate estate rather than community estate).

➤ **Comment.** A Wisconsin court interpreting an interspousal remedy under section 766.15 would probably rule consistently with *Noble* and *Somps*, both divorce cases, and find that a spouse does not violate the good-faith duty by failing to take advantage of an opportunity that would enhance the marital property of the spouses.

## 2. Definition of the Duty [§ 8.12]

The Act created a new duty between spouses in section 766.15: (1) Each spouse shall act in good faith with respect to the other spouse in matters involving marital property or other property of the other spouse....

The term *good faith* is not defined in the Act. However, statutes and case law developed in other areas may help by analogy to provide a definitional framework, subject to limitations that result from the unique relationship between spouses. Good faith under the Uniform Commercial Code, for example, is defined as “honesty in fact in the conduct or transaction concerned,” Wis. Stat. § 401.201(19), and as “honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.” Wis. Stat. § 402.103(1)(b). Mere negligence appears not to be actionable, although it is arguable that reckless disregard by one spouse of the rights of the other spouse may constitute a breach of the duty.

Under an early version of the Act, a spouse was obligated to act in a way that he or she reasonably believed was either in or not opposed to the best interests of the marriage and in a way that did not use the marital property or the property of the other spouse to the advantage of the managing spouse and to the detriment of the other spouse. Wis. Assem. Substitute 4 to 1979 A.B. 1090, section 48 (creating section 766.13(3)).

This version of the good-faith duty was replaced by the standard in the Uniform Marital Property Act (UMPA, reprinted in appendix A, *infra*). The comment to UMPA section 2 explains the duty as follows:

Spouses are not trustees or guarantors toward each other. Neither are they simple parties to a contract endeavoring to further their individual interests. The duty is between, and is one of good faith. A spouse is not bound always to succeed in matters involving marital property ventures, but while endeavoring to succeed in a venture, must proceed with an appropriate regard for the property interests of the other spouse and without taking unfair advantage of the other spouse.

The express language of section 766.15(1) and of the Committee Note to section 766.70(1) makes clear that the duty exists with respect to both the interest of the other spouse in marital property and the other spouse's nonmarital property. *See* Wis. Stat. Ann. § 766.70 Legis. Council. Comm. Supplemental Notes Relating to 1985 Act 37 (West 2009) (concerning the remedy for breach of the duty of good faith).

### **3. Analogy to Other Community Property States** **[§ 8.13]**

Historically, the husband in other community property states was the sole manager of all community property, although some states required joinder by the wife for the alienation of real property. *See* William Q. de Funiak & Michael J. Vaughn, *Principles of Community Property* § 113 (2d ed. 1971); W.S. McClanahan, *Community Property Law in the United States* § 9:12 (1982 & Supp. 1992). Courts in community property states developed rules that were protective of the wife's interest in community property because she could do nothing to manage and control that property to protect her interest. In older cases, courts often imposed the fiduciary standards of a trustee although not the trustee's duty to account specifically for each transaction involving community property. Reppy & Samuel, *supra* § 8.8, at 245–46. In a 1971 case, a California appellate court described the extent of the husband's duty as follows:

It would seem that a husband's duty not to obtain an unfair advantage over his wife by reason of his control of the community property does not require that the husband be as prudent as a trustee or that he keep complete and accurate records of income received and disbursed.



*Williams v. Williams*, 92 Cal. Rptr. 385, 389 (Ct. App. 1971); *see also* *Vai v. Bank of Am. Nat'l Trust & Sav. Ass'n*, 364 P.2d 247 (Cal. 1961) (“The key factor in the existence of a fiduciary relationship lies in control by a person over the property of another.”).

Resort to the court system should not be used for minor wrongs by spouses. *de Funiak & Vaughn, supra*, at § 120. However, immoderate gifts or expenditures of community property for immoral purposes would give rise to a remedy. *Id. But see infra* § 8.45 (discussion of the remedy under the Act relating to gifts of marital property).

Within the last several decades, all the original community property states enacted statutes giving husbands and wives equal management and control of community property, with some limited exceptions. *McClanahan, supra*, § 9:12 at 466–72. This right of equal management and control gives each spouse a means, probably more theoretical than practical, to protect his or her interest in community property without court intervention. As a result of this change, the courts in most community property states have been less likely to hold spouses to the strict fiduciary standards of a trustee. *Reppy & Samuel, supra* § 8.8, at 245–46. Rather, both case law and statutes have tended to require only a duty of honesty and good faith. *Id. But see* the discussion of the spouse’s duties under California law, *infra*.

Good faith, in contrast to the fiduciary duty of a trustee, does not require wisdom in investing. Losses as well as gains accrue to the marital estate as long as a benefit was intended. *See Peters v. Skelman*, 617 P.2d 448, 452 (Wash. Ct. App. 1980); *see also Hauge v. Hauge*, 145 Wis. 2d 600, 603–05, 427 N.W.2d 154 (Ct. App. 1988).

Spouses are not required to give every advantage to the community. For example, in *Somps v. Somps*, 58 Cal. Rptr. 304 (Ct. App. 1967), which was decided before enactment of the good-faith statute in California, Cal. Fam. Code § 1100(e) (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot), the husband took advantage of an investment opportunity by using his separate funds rather than community funds. The court found no breach of duty because, it said, the husband was not required to allow his separate estate to remain uninvested to give every advantage to the community. 58 Cal. Rptr. at 309–11.

A stricter standard of good faith may be imposed on spouses who are separated or for whom a divorce is pending, because the concept of the spouses' unity of purpose may no longer be valid. *Reppy & Samuel, supra* § 8.8, at 244–45. Thus, in *Ogden v. Ogden*, 331 So. 2d 592, 597 (La. Ct. App. 1976), the court found that the separated husband who acquired the right to exercise an investment opportunity by reason of ownership of community stock violated his duty to the community by purchasing the stock as his separate property.

Most of the cases involving breach of the good-faith duty in community property states arise in the divorce context. California, for example, divides community property equally at divorce and awards each spouse his or her separate property. Cal. Fam. Code § 2550 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot). Equitable considerations are not applied; however, one spouse may recover more than his or her share of community property from the share allocated to the other spouse if the claimant spouse can prove that the other spouse “deliberately misappropriated” property to the exclusion of the claimant’s community property interest. Cal. Fam. Code § 2602 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot). Deliberate misappropriation would certainly give rise to a claim for breach of the good-faith duty under the Act. However, the good-faith duty under the Act is broader than deliberate misappropriation. Thus, California decisions finding deliberate misappropriation may be helpful. Even though deliberate misappropriation was not found under the facts in a California case, *see Schultz v. Schultz*, 164 Cal. Rptr. 653 (Ct. App. 1980) (finding no deliberate misappropriation in spouse’s failing to defend lawsuit and allowing default judgment obligating community), similar facts may nevertheless constitute a breach of the good-faith duty under the Act.

On the other hand, Texas does not allow a separate tort action between spouses for fraud with respect to community property and instead restricts remedies for fraud to an unequal property division at divorce. *Schlueter v. Schlueter*, 975 S.W.2d 584 (Tex. 1998).

Other cases have analyzed the duty of spouses with respect to management of undivided community property after marital dissolution.

For example, in *Terry v. Terry*, 565 So. 2d 997 (La. Ct. App. 1990), the court interpreted Louisiana Civil Code article 2354 and held that the good-faith duty in management of community property exists until partition. The husband violated this duty by liquidating a community property corporation and used a substantial portion of the resulting funds for a pension for himself, thus depleting the corporation's value, without informing the wife. Other cases involve postjudgment attacks on allegedly unfair marital settlement agreements that were procured by one spouse who had concealed community property at the time of the divorce. See, e.g., *In re Stanifer*, 236 B.R. 709 (9th Cir. B.A.P. 1999) (holding that existence of marriage created fiduciary duty between spouses under California law); *Stevenot v. Stevenot*, 202 Cal. Rptr. 116 (Ct. App. 1984) (summarizing cases relating to historical fiduciary duty that preceded statutory creation of good-faith duty between spouses and equal spousal rights of management and control); see also *Alexander v. Alexander*, 261 Cal. Rptr. 9, 13 (Ct. App. 1989) (noting that post-*Stevenot* statutory amendment extended good-faith duty beyond separation to final judgment, even though property acquired after separation is separate, not community, property); *Baltins v. Baltins*, 260 Cal. Rptr. 403, 417 (Ct. App. 1989) ("Each party is bound in transactions with the other to the highest and best of good faith and is obligated not to obtain and retain any advantage over the other resulting from concealment or undue pressure."). The higher fiduciary standard now imposed by statute may be similar to the fiduciary good-faith duty that existed before enactment of statutes granting equal management and control of community property.

As noted earlier, the other community property states generally grant husbands and wives equal management and control of community property, subject to a number of exceptions. The Act, however, does not. Under the Act, a spouse may manage and control all of his or her nonmarital property and all marital property that is held in that spouse's name alone or that is in the spouse's possession and is untitled. Wis. Stat. § 766.51(1)(a), (am). Either spouse acting alone may manage marital property held by both spouses in the alternative (i.e., A *or* B). Wis. Stat. § 766.51(1)(b). For the purpose of obtaining an extension of unsecured credit for a family-purpose obligation, each spouse may manage all marital property with the exception of interests in certain types of business property. Wis. Stat. § 766.51(1m). Each spouse may manage life insurance for which he or she is the owner on the issuer's records, employee-benefit plans that accrue by reason of that spouse's

employment, and any claim for relief that vests in that spouse by any law other than the Act. Wis. Stat. § 766.51(1)(d), (e), (f).

When held by one spouse, the management and control rights under the Act are closely analogous to the historical management and control rights held solely by the husband. The spouse who does not “hold” marital property does not have a direct right of access to that property without court intervention. This contrasts with the equal right of each spouse under current law in other community property states to manage and control all community property, subject to exceptions for certain types of property. If the Act provided no other remedies, the good-faith duty imposed by section 766.15(1) would probably be insufficient to protect the nonmanaging spouse who disagrees with actions taken in good faith by the managing spouse concerning marital property. To afford adequate protection, the standard of conduct would probably have to be closer to the fiduciary standard imposed by the community property states before equal management and control became the rule.

However, the Act provides other interspousal remedies to supplement the action under section 766.70(1) for breach of the good-faith duty. These remedies include a right to an accounting and (with certain exceptions) access to marital property in the hands of the other spouse or the other spouse’s transferee. Wis. Stat. § 766.70(2)–(8); *see infra* §§ 8.44–.59. These additional remedies, in contrast to the remedy for breach of the good-faith duty, do not always require wrongdoing by the managing spouse. It is arguable that the right to recover marital property under these other remedies is similar to the right of control by a nontitled spouse in a community property state having equal management and control. Therefore, court decisions in community property states after the adoption of equal management and control may be useful in interpreting the good-faith duty in Wisconsin. However, cases from other community property states involving alleged violations of the good-faith duty should be read in the context of any applicable good-faith statutes in that state. For example, Louisiana’s statute is similar to section 766.15(1), and California’s statute is not. *See* La. Civ. Code Ann. art. 2354 (WESTLAW current through the 2009 regular session) (“A spouse is liable for any loss or damage caused by fraud or bad faith in the management of community property.”); Cal. Fam. Code §§ 1100(e), 721 (WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot) (imposing fiduciary duty higher than good-faith

standard). In cases decided under California's good-faith statute, Cal. Fam. Code § 1100(e), the fact situations appear to relate more to particular remedies under the California statutes than to the general good-faith duty. Typically, these cases include either recovery from the other spouse or from a recipient of community property transferred by one spouse without the other spouse's consent, or reimbursement for debts incurred by one spouse before the marriage and satisfied with community property. These situations are discussed in the relevant sections of this book. Section 1101 of the California Family Code (WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot) provides for remedies between spouses during the marriage, a number of which are similar to section 766.70.

#### **D. Exception to Duty of Good Faith [§ 8.14]**

A spouse's good-faith duty in matters involving marital property does not extend to matters involving that spouse's individual and predetermination date property. A spouse is free to manage and control that property in any manner, even though income (which is marital property unless one of the exceptions listed in section 2.63, *supra*, applies) is diminished or nonexistent. Wis. Stat. § 766.15(2). The comment to UMPA section 2 makes clear that a spouse may regulate the income of his or her nonmarital property without violating the good-faith duty.

### **III. Actions Between Spouses [§ 8.15]**

#### **A. In General [§ 8.16]**

The creation of the marital property system of co-ownership not only resulted in the imposition of new duties regarding the property of the spouses, it also resulted in the creation of new causes of action to enforce those duties. The actions discussed in this chapter relate to statutorily created actions between spouses. Marital property agreements, other marriage agreements, and the enforcement of such agreements are discussed in chapter 7, *supra*. In addition to the previously existing cause of action to enforce support under section 767.501, independent causes of action arise under section 766.70. Each of these actions may

be commenced separately, or several may be commenced simultaneously, depending on the circumstances giving rise to the claim. Certain actions discussed in sections 8.44–.59, *infra*, may be commenced against a third party, the other spouse, or a third party and the other spouse. The measure of damages is discussed in section 8.38, *infra*. An interspousal remedy may not be commenced if an action for dissolution is pending. Wis. Stat. § 767.331; *see infra* § 8.61.

Remedies under section 766.70 are intended to affect only the rights of the spouses in relation to each other. Except under limited circumstances, a decree under section 766.70 may not adversely affect the rights of third parties. Wis. Stat. § 766.70(8). Third parties who may be affected include donees of a spouse, creditors with actual knowledge or a copy of a decree before extending credit, and certain purchasers from a spouse. *Id.*

Remedies under section 766.70 apply only to marital property and not to predetermination date property (regardless of whether such property is within the definition of deferred marital property) or other nonmarital property of the managing spouse.

There may be actions between spouses involving rights that do not arise under section 766.70 that can be maintained separately from an action under section 766.70 or from an action for dissolution. *See, e.g., Jezo v. Jezo*, 23 Wis. 2d 399, 127 N.W.2d 246 (1964) (allowing action for partition of joint-tenancy property); *Knafelc v. Dain Bosworth, Inc.*, 224 Wis. 2d 346, 591 N.W.2d 611 (Ct. App. 1999) (permitting claim of securities-fraud violations); *Caulfield v. Caulfield*, 183 Wis. 2d 83, 515 N.W.2d 278 (Ct. App. 1994) (allowing separate action on note); *Stuart v. Stuart*, 140 Wis. 2d 455, 410 N.W.2d 632 (Ct. App. 1987), *aff'd*, 143 Wis. 2d 347, 421 N.W.2d 505 (1988) (allowing separate action for assault, battery, and intentional infliction of mental distress); *see also* Nadine E. Roddy, *The Interspousal Tort Suit: A New Avenue of Recovery for Marital Misconduct*, 7 Divorce Litig. 213 (Oct. 1995).

## **B. To Compel Support [§ 8.17]**

Although seldom used, section 767.501 provides for an independent cause of action that one spouse may commence against the other for support during an ongoing marriage. Since this is an action affecting the family, *see* Wis. Stat. § 767.001, procedures are as outlined in chapter

767. The general procedural statutes, chapters 801 to 807, govern actions under section 766.70. Typically, the action for support under section 767.501 has been used by child-support agencies to collect reimbursement of public funds. However, it appears that it could be used by one spouse attempting to obtain support from the other spouse. The amount of support is not limited to subsistence but is determined by the guidelines under sections 767.511 and .56, which enumerate the considerations for determining child support and spousal maintenance, respectively.

### **C. Breach of Good-faith Duty [§ 8.18]**

Since each spouse owes a duty to the other to act in good faith in matters relating to their marital property and to each other's nonmarital property, it follows that a cause of action arises when one spouse breaches that duty. Section 766.70(1) provides, in part, that "[a] spouse has a claim against the other spouse for breach of the duty of good faith imposed by s. 766.15 resulting in damage to the claimant spouse's property." This remedy is available for any of a spouse's property damaged by the other spouse in violation of the duty, not just marital property. Wis. Stat. Ann. § 766.70(1) Legis. Council Comm. Supplemental Notes Relating to 1985 Act 37 (West 2009); *see also supra* § 8.12. An action under section 766.70(1) is independent of other claims one spouse may have against his or her spouse, although it may be combined with other claims.

A remedy is available only if the breach results in damage to the spouse's property, thereby eliminating from this action many interspousal wrongs that have no economic consequences. These might include interspousal actions for personal injury inflicted by one spouse on the other spouse, actions that are beyond the scope of this discussion. *See, e.g., Stuart v. Stuart*, 140 Wis. 2d 455, 410 N.W.2d 632 (Ct. App. 1987), *aff'd*, 143 Wis. 2d 347, 421 N.W.2d 505 (1988); *see also supra* § 2.134 (interspousal tort liability); *infra* §§ 8.41 (guarantees), .63 (sample forms).

The general civil-procedure statutes in chapters 801 to 807, including the right to trial by jury, apply to cases under section 766.70. *See infra* §§ 8.60–.62. Allegations in the complaint attempting to establish a breach of the good-faith duty should state that the plaintiff and the defendant are married to each other and that no action for dissolution is

pending, describe the transactions or course of conduct causing the damage, specify the damage, and state the relief requested. If fraud is pleaded, it must be described with specificity. Wis. Stat. § 802.03(2). Other remedies under section 766.70 may also be available under a particular set of facts.

The courts decide on a case-by-case basis what kinds of wrongful conduct give rise to a remedy under section 766.70(1). For example, in *Lloyd v. Lloyd*, 170 Wis. 2d 240, 264, 487 N.W.2d 647 (Ct. App. 1992), the court stated that the decedent's act of transferring bank accounts of marital property funds in violation of a court order while his divorce was pending constituted a violation of his good-faith duty. It appears that certain intentional acts causing damage to property of another person that would be actionable under common law property rules with respect to third parties would also be actionable between spouses under section 766.70(1). Acts of fraud or conversion are examples. In addition, acts that constitute unfair advantage and abuse of a confidential relationship, but that would not necessarily constitute an intentional tort if committed against a third person, may also constitute a breach of the good-faith duty. This might include granting a security interest in marital property to secure a debt that is not in the interest of the marriage or the family. Another example may be converting marital property (without the right of survivorship) into survivorship marital property to defeat the other spouse's testamentary power to will his or her interest in marital property. See *supra* ch. 4; see also Patrick K. McDaniel, *Claims and Remedies for Violation of Fiduciary Duty*, 15 Divorce Litigation 1 (Jan. 2003).

Finally, several remedies under section 766.70(1) are based on conduct of a spouse that would not have been actionable before the Act. These include, for example, a cause of action for failure of a spouse to protect the other spouse's property by failing to disclose to a creditor a marital property agreement, a unilateral statement under section 766.59, or a decree under section 766.70. The result of such failure is that the creditor is not bound by the terms of the undisclosed document under section 766.55(4m), and the nonincurring spouse's property may be recovered by the creditor in satisfaction of the nondisclosing spouse's obligation. Falsely signing the conclusive family-purpose statement under section 766.55(1) to obtain credit for other than a family purpose or failing to serve a unilateral statement under section 766.59 on the other spouse may also constitute a breach of the good-faith duty if economic damage results.



Certain conduct may be valid in some cases and actionable in others, depending on intent and whether damage results. For example, a spouse's execution of a guarantee that does not benefit the spouses may adversely affect the parties' credit and ability to conduct business, even though no default by the third-party principal has occurred and no payment with marital property has been made. *See supra* §§ 4.59, 6.22 (discussing the effect of guarantees executed by one spouse). Under some circumstances, one spouse's preemptive use of available credit may have the same result. *See supra* ch. 5 (discussing creditworthiness and the other spouse's exercise of management and control rights). Control of some assets may be governed by federal preemption. *See supra* §§ 2.211–.217, .265–.270. Provisions in a buy-sell agreement may improperly diminish a spouse's rights. *See supra* §§ 4.79–.84 (discussion of management and control in entering into buy-sell agreements). The concept of good faith is flexible and can be applied by the court to achieve equity.

A spouse bringing an action under section 766.70(1) must commence the action no later than six years after acquiring actual knowledge of the facts giving rise to the claim. An exception to this limitation is found in section 766.70(6)(a), relating to recovery from the other spouse (or from a third party) for completed unauthorized gifts of marital property. *See infra* § 8.45. An action under section 766.70(6)(a) must be brought within one year after the spouse has notice of the gift, within one year after a dissolution, or within the time limit for filing claims after the death of either spouse, whichever is earliest. Wis. Stat. § 766.70(6)(a).

There may be instances in which wrongful conduct by a spouse gives rise to an action for breach of the good-faith duty under section 766.70(1) as well as under another, more specific subsection of section 766.70. For example, payment of a nonfamily purpose obligation with marital property, perhaps because the incurring spouse falsely signed a statement of family purpose under section 766.55(1), could permit recovery under subsections 766.70(5) and (1). Section 766.70(5) has a limitation period of only one year from the satisfaction of the obligation. The better rule appears to be that even though the disputed conduct could fit under either section 766.70(1) or (5), the specific statute takes precedence over the general statute. Therefore, the shorter limitation period cannot be avoided by using the more general remedy under section 766.70(1), which has a six-year limitation period.

**D. Accounting; Determination of Ownership;  
Classification of Property; Beneficial Enjoyment of  
or Access to Marital Property [§ 8.19]**

**1. Accounting [§ 8.20]**

Section 766.70(2) provides for a variety of interspousal remedies: (2) Upon request of a spouse, a court may order an accounting of the spouses' property and obligations and may determine rights of ownership in, beneficial enjoyment of or access to marital property and the classification of all property of the spouses.

Section 766.70(2) provides that a spouse may require an accounting of marital property at any time during the ongoing marriage simply by bringing such an action. Traditional community property law does not provide a right to an accounting during the marriage; rather, the right arises only on termination of the marriage. *See supra* § 4.32; *but see McClung v. Smith*, 870 F. Supp. 1384 (E.D. Va. 1994) (holding that existence of marriage does not bar remedy of accounting when husband managed wife's assets), *aff'd in part, remanded in part*, No. 95-1106, No. 95-1187 (4th Cir. June 19, 1996). Generally, in an action for an accounting the court may require a spouse to disclose the nature and location of marital property assets under his or her control and the circumstances under which such assets were disposed of. The request for an accounting may be combined with a request for damages for breach of the good-faith duty, reimbursement, or other relief if the accounting reveals wrongful conduct for which a spouse is answerable. An accounting may also be necessary to invoke other remedies in section 766.70.

Since none of the remedies under section 766.70 is possible without disclosure, a duty of full disclosure at all times during marriage must be inferred. This duty is different from the duty to disclose the existence of property owned by a spouse at the time of making a marital property agreement, Wis. Stat. § 766.58(6)(c), and at the time of divorce, Wis. Stat. §§ 767.127(1), .63. *See also supra* §§ 8.7–8.

In *Brassett v. Brassett (In re Brassett)*, 332 B.R. 748 (Bankr. M.D. La. 2005), the court dealt with a managing spouse's duty to account to a nonmanaging spouse with respect to unpartitioned community property under Louisiana law. The issue arose when the former wife filed a

bankruptcy petition after a divorce and before the community property was partitioned. Under bankruptcy law, all community property becomes part of the bankruptcy estate when one spouse files, and unpartitioned community property after divorce is treated in the same manner. *See* 11 U.S.C. § 541(a)(2); *see also supra* §§ 6.74–.77. The nonfiling former husband argued that distributions from a community property joint venture were earned income, which would have been his separate property, but the court held that these were equity distributions of a community property business. Accordingly, all community property assets became part of the wife’s bankruptcy estate, and her right to an accounting and recovery of community property distributions received by the husband also passed to her estate.

## 2. Ownership; Classification [§ 8.21]

Under section 766.70(2), a spouse may ask the court to classify the parties’ property if the classifications are unclear or if the parties disagree. Wis. Stat. § 766.70(2); *see supra* ch. 2 (discussion of property classifications). No grounds for relief are required. Such an action may be appropriate to add certainty to estate planning, to clarify ownership for business or credit purposes, and to determine ownership in other situations.

Classification as it exists at the time of the decree is determined by the court. An action under section 766.70(2) does not authorize change from one classification of property to another. The comment to UMPA section 15, which provides for this remedy, indicates that such an action allows a balancing of property rights and should allow for the balancing of gains and losses. This comment apparently means that the aggregate of marital property may be classified and there would not necessarily be an item-by-item allocation of interests. The remedy under section 766.70(2) also may be used for “unmixing” property with marital and nonmarital components. UMPA § 15 cmt.

Only a spouse can require an accounting as an interspousal remedy under section 766.70(2). *See* Wis. Stat. Ann. § 766.70 Legis. Council Notes—1985 Act 37, §§ 89, 130 to 138 (West 2009). An accounting or determination of classification is not available to third parties, such as creditors. However, the need for such a remedy may be triggered by a creditor’s attempt to recover from property that the creditor claims is

marital property but that the nonincurring spouse can prove is his or her nonmarital property. *See also supra* ch. 3.

### **3. Beneficial Enjoyment; Access [§ 8.22]**

Section 766.70(2) permits a determination of the right of a spouse to beneficial enjoyment of or access to marital property. No grounds are stated and apparently none are needed. Access and beneficial enjoyment connote management and control, although grounds involving some kind of misconduct are required to limit management and control. *See* Wis. Stat. § 766.70(4). It appears that this remedy could be used to provide a right to use marital property notwithstanding the fact that the property is held by the other spouse, provided that the spouse who holds the property is not deprived of management and control. A determination of rights under this subsection may also settle who may use marital or mixed property such as an automobile or a vacation home.

## **E. Add a Name to Marital Property [§ 8.23]**

### **1. In General [§ 8.24]**

Marital property held in the name of one spouse is subject to his or her exclusive management and control, except in certain credit transactions. Wis. Stat. § 766.51(1m). To prevent abuse of the right of exclusive management, or to provide control by both spouses, section 766.70(3) provides that except for certain business interests, *see infra* § 8.26, a spouse can have his or her name added to marital property or to the document evidencing ownership. If the name is added in the conjunctive (i.e., A *and* B), both spouses must act together to manage and control that asset. Wis. Stat. § 766.51(2). This provides joint control or at least gives veto power to the spouse who previously had no control. The comment to UMPA section 15 states that this is the primary purpose of the remedy.

If a separated spouse is concerned that a marital property asset, such as a large cash or brokerage account, will be dissipated before a property division in a dissolution action is completed, then before the dissolution action is commenced, the spouse can attempt to use section 766.70(3) to prevent the loss. This provides a measure of direct control to the previously nonmanaging spouse. Joint control may be preferable to a

temporary restraining order set by the court under section 767.225(1). A temporary restraining order typically provides that the parties may not dispose of property or remove it from the state. *See* Wis. Stat. § 767.225(1)(h); *see also* Wis. Stat. § 767.117(1)(b). It is not always clear during separation whether expenditures of marital property by the managing spouse are for legitimate purposes or whether they constitute unreasonable dissipation or unfair use of marital property funds for the exclusive benefit of the managing spouse. The add-a-name remedy gives both spouses the right to control such decisions. Joint action by both spouses is also more flexible than freezing an account because the parties can confer and agree on expenditures to be made.

It must be noted, however, that section 767.331 prohibits commencing an action for any remedy under section 766.70 once an action under chapter 767 has been filed. *See also Gardner v. Gardner*, 175 Wis. 2d 420, 499 N.W.2d 266 (Ct. App. 1993); *Haack v. Haack*, 149 Wis. 2d 243, 440 N.W.2d 794 (Ct. App. 1989). Actions between spouses involving rights other than those that arise under section 766.70 may continue to be available. *Knafelc v. Dain Bosworth, Inc.*, 224 Wis. 2d 346, 591 N.W.2d 611 (Ct. App. 1999). If a dissolution is subsequently commenced and consolidated with the add-a-name action, it does not appear that there is conflict with any provision in chapter 767. If there is, chapter 767 supersedes section 766.70. Wis. Stat. § 767.331; *see infra* § 8.61 (discussion of *Haack*); *see also Gardner*, 175 Wis. 2d at 425–33.

Section 766.70(3) specifies no grounds for applying the remedy. The court will probably order the name of the spouse added unless the rights of the other spouse or a third party would be jeopardized, unless there are excepted business interests involved, or unless the petitioning spouse has only a minimal interest in the property (for example, if the property is mixed property that is primarily nonmarital in character). Also, a remedy under section 766.70(3) is probably not available with respect to the earnings of an employee spouse. *See infra* § 8.40.

The add-a-name remedy is only available with respect to marital property assets held solely in the name of the other spouse. Wis. Stat. § 766.70(3). If assets are transferred to a revocable trust, for example, the remedy is not available, even though the assets continue to be classified as marital property when held by the trustee. *See* Wis. Stat. § 766.31(5); *see also infra* ch. 10. The nontitled spouse may have other remedies during the transferor's lifetime, however, such as an action for

breach of the good-faith duty. Wis. Stat. §§ 766.15, .70(1); *see also supra* § 8.18.

In addition to protecting a spouse's interest in assets, section 766.70(3) may arguably be used in place of a guardianship, unless excepted business interests are involved, *see* Wis. Stat. § 766.70(3)(a)–(d), or if the rights of third persons would be adversely affected, *see* Wis. Stat. § 766.70(3)(e). The statute does not state that the name of the petitioning spouse must be added in the conjunctive (i.e., *A* and *B*), and thus it appears that adding the name in the alternative (i.e., *A* or *B*) may also be permitted. If one spouse is incompetent, it may be desirable for the name of the other spouse to be added in the alternative to marital property held by the incompetent spouse. The managing spouse is subject to a good-faith duty, but the time and administrative costs of a guardianship are avoided. It would also be possible for the managing spouse to make reasonable gifts under section 766.53 for estate-planning purposes, which a guardian could not make without court approval.

Although adding a name in the alternative theoretically does not diminish the rights of the spouse who originally held the property (because property held in the alternative may still be managed by either spouse acting alone), it may do so as a practical matter. It is arguable that this statute is not intended to deprive a spouse of management and control. This argument is based on section 766.70(4), which requires a finding of gross mismanagement, waste, or absence to limit a spouse's management and control under that section. Whether it is permissible to add the name of a spouse in the alternative will probably be clarified by statutory revision or judicial interpretation.

## **2. Exceptions [§ 8.25]**

### **a. Business Assets [§ 8.26]**

The add-a-name remedy provided by section 766.70(3) is not available for certain business interests that are marital property and that are held only by the spouse who is active in the business. The purpose of this exception is to allow the spouse who is knowledgeable about a business to operate it independently of the other spouse (subject to the duty of good faith), notwithstanding the marital property interest of the nonparticipating spouse.

The excepted business interests are as follows:

(a) An interest in a partnership [either general or limited] or joint venture held by the other spouse as a general partner or as a participant.

(aL) An interest in a limited liability company held by the other spouse as a member.

(b) An interest in a professional corporation, professional association or similar entity held by the other spouse as a stockholder or member.

(c) An asset of an unincorporated business if the other spouse is the only one of the spouses involved in operating or managing the business.

(d) A corporation, the stock of which is not publicly traded. Under this paragraph, stock of a corporation is publicly traded if both of the following apply:

1. The stock is traded on a national stock exchange or quoted on the national association of securities dealers' automated quotations system.

2. The employees, officers and directors of the corporation own, in the aggregate, less than 10% in value of the outstanding shares of the stock in the corporation.

Wis. Stat. § 766.70(3)(a)–(d).

Before passage of 1987 Wisconsin Act 393 [hereinafter 1988 Trailer Bill], section 766.70(3)(d) required that a spouse who holds stock in a closely held corporation also be employed by the corporation for the exception to apply. Under the modified section 766.70(3)(d), the add-a-name remedy is not available, regardless of whether the holding spouse is an employee.

## **b. Nonbusiness Assets [§ 8.27]**

The add-a-name remedy under section 766.70(3) is not allowed if the rights of a third party would be adversely affected. Wis. Stat. § 766.70(3)(e). For example, creditors or other parties may have negotiated or taken action in reliance on the management and control of one spouse; on this basis they may have changed their positions with respect to sales, extensions of credit, joint ventures, or other transactions. It would be unfair to adversely affect the rights of a third person by changing management and control after the third person has relied on the control of the spouse holding the property.

## **F. Limitation of Rights of Management and Control; Change of Classification; Categorization of Present and Future Obligations and Property [§ 8.28]**

### **1. In General [§ 8.29]**

The remedies set forth in sections 8.18–.27, *supra*—namely, bringing an action for breach of the good-faith duty, requiring an accounting for marital property, and adding a name to marital property—are the only interspousal remedies in UMPA. The Act provides additional remedies between spouses and others.

A group of these additional remedies is under section 766.70(4). Each remedy relates to potential or actual damage to marital property and requires proof of gross mismanagement, waste, or absence by or of a spouse. Poor judgment or ineptness is apparently insufficient to support these remedies. There must be proof that substantial injury to marital property has occurred or is likely to occur in the future. Mere disagreement as to how property should be managed, without proof that substantial damage has occurred or will occur, does not support the action. Relief would not necessarily involve all marital property, but only that part of the marital property subject to the specified harm.

Under section 766.70(4), a spouse can ask the court to limit or terminate the other spouse's management and control rights to marital property. Wis. Stat. § 766.70(4)(a)1. The limitation can be temporary or permanent. *Id.* The court can change the classification of marital property owned by the spouses, Wis. Stat. § 766.70(4)(a)2., and can determine that property to be acquired by the spouses after entry of the order is the acquiring spouse's individual property, Wis. Stat. § 766.70(4)(a)5. Obligations can be divided after consideration of the categories of obligations under section 766.55(2) and the factors applicable to the parties under sections 767.56 and .61. Wis. Stat. § 766.70(4)(a)3. Responsibility for payment and property available for payment of future obligations can be determined. Wis. Stat. § 766.70(4)(a)4. Certain types of marital property assets related to a business in which one spouse has an interest may not be reached under this section. Wis. Stat. § 766.70(4)(c); *see infra* § 8.35. Finally, remedies under section 766.70(4) may be subject to any equitable condition. Wis. Stat. § 766.70(4)(b). The various remedies under section 766.70(4) are discussed in more detail below.



## 2. Limitation or Termination of Management and Control [§ 8.30]

The court can limit or terminate one spouse's management and control of marital property without changing ownership. Wis. Stat. § 766.70(4)(a)1. The change can be temporary or permanent, *id.*, and can be subject to any equitable condition, Wis. Stat. § 766.70(4)(b). *See supra* § 4.58 (disability or absence of spouse).

This remedy may be useful if a guardianship would be too cumbersome or not appropriate. For example, it may be used if one spouse is suffering from alcoholism or other chemical dependency, which may or may not be a permanent problem and may result in gross mismanagement, although the spouse falls short of legal incompetency. Also, annual accounts, restrictions on investments, and other requirements or limitations of legal guardianships are avoided. Certain protections under chapter 54 are lacking, however, such as mandatory appointment of a guardian ad litem, although it appears necessary to request that a guardian ad litem be appointed if the spouse's ability to respond is impaired. *See* Wis. Stat. § 803.01(3).

If the marital property asset subject to an action under section 766.70(4) is a deferred-employment-benefit plan to which 29 U.S.C. § 1056(d) (restriction on alienation of qualified plans) applies, a qualified domestic-relations order (QDRO) may be appropriate to require the plan administrator to pay benefits to the beneficiary's spouse. The term *domestic relations order* includes an order that relates to marital property rights and is made under state domestic-relations law, including a community property law. 29 U.S.C. § 1056(d)(3)(B)(ii). Although the Ninth Circuit Court of Appeals in *Ablamis v. Roper*, 937 F.2d 1450 (9th Cir. 1991), held that a probate court order may not qualify as a domestic-relations order and that general community property orders other than those related to family support generally do not qualify as domestic-relations orders, remedies of the types described in section 766.70 were not addressed. *See also* Wis. Stat. § 765.001(1) (chapter 766 is part of the Family Code).

The good-faith duty applies to the spouse who acquires management rights under this section, but the standard of care is less than the fiduciary standard applicable to a guardian. *See supra* § 8.18; *see also* Wis. Stat.

§§ 54.19–.21 (duties and powers of guardian of estate of incompetent person).

### **3. Change in Classification of Property [§ 8.31]**

Certain remedies under section 766.70, other than section 766.70(4), specify particular instances in which the classification of property may be changed, usually to award individual property to a spouse damaged by the other spouse's misuse of marital property. *See* Wis. Stat. § 766.31(7)(e). These include remedies for breach of the good-faith duty, for gifts in excess of value limits, and for use of marital property to pay obligations that are other than family-purpose obligations. *See supra* § 8.18, *infra* §§ 8.36, .45. The remedy under section 766.70(4)(a)2. for a change of classification of marital property could be used when these other remedies do not apply but gross mismanagement, waste, or absence, with resulting potential or actual damage to marital property, has occurred.

It should be noted that under section 766.70(4)(a)2., the court can only change the classification of marital property; the court cannot transfer the nonmarital property of one spouse to the other.

It appears that section 766.70(4)(a)2. is unavailable to provide relief for a spouse who wishes merely to obtain an order that reclassifies marital property accumulated during a separation as the individual property of the spouse who acquired it, unless proof of substantial injury to the property or the spouse's property interest is shown. Without such proof, the transfer of ownership of marital property requires the agreement of the spouses or an award of property upon dissolution. *But see infra* § 8.34 (classification of property acquired in the future).

Any change in the classification of assets by decree may not adversely affect a creditor whose rights arose before the decree or after the decree, if the creditor had no notice of the decree or was not provided a copy before the credit was granted. Wis. Stat. § 766.55(4m).

### **4. Division of Existing Obligations [§ 8.32]**

Under section 766.70(4)(a)3. a spouse may request that the court divide existing obligations. This remedy may not adversely affect the

rights of existing creditors because they would not have had notice of the order before extending credit. Wis. Stat. §§ 766.55(4m), .70(8). Creditors who did not have notice of the order before extending credit may seek satisfaction from the same sources and classifications of property available before the order assigning obligations was entered.

In dividing the spouses' obligations, the court must apply the same standards used in an action for dissolution to determine property division, *see* Wis. Stat. § 767.61, and maintenance, *see* Wis. Stat. § 767.56. Wis. Stat. § 766.70(4)(a)3. Although these standards are more suitably applied to assets than to obligations, each spouse's access to income and assets will be considered in determining an equitable allocation of obligations. For example, obligations described in section 766.55(2)(c) that were incurred before the marriage or before January 1, 1986, would probably be assigned to the spouse who incurred them, just as property brought to the marriage by a spouse is more likely to be assigned to that spouse. Wis. Stat. § 767.61(2). Obligations that were not incurred in the interest of the marriage or the family, Wis. Stat. § 766.55(2)(d), would probably be assigned to the incurring spouse after the court considered the negative contributions (i.e., acts that diminish the assets subject to division) of that spouse to the marriage. Wis. Stat. § 767.61(3); *see also Anstutz v. Anstutz*, 112 Wis. 2d 10, 331 N.W.2d 844 (Ct. App. 1983). Family-purpose debts under section 766.55(2)(b) may be assigned to either spouse after the court considers such factors as the spouses' respective earning capacities, work experience, training, and responsibility for caring for minor children. *See* Wis. Stat. §§ 767.56(5), .61(3).

Although section 766.55(2m) provides that a creditor has a direct cause of action against the spouse who is assigned an obligation in a dissolution proceeding, there is no similar provision allowing a creditor to sue the spouse assigned the obligation under section 766.70(4)(a)3. Since an order under this subsection affects obligations incurred before the entry of the order, existing creditors are not bound by an adverse provision. Wis. Stat. § 766.55(4m). If the creditor is otherwise able to sue the assigned spouse directly, which is permitted by section 803.045, there are no adverse consequences to an existing creditor because of an order under section 766.70(4)(a)3.

## **5. Assignment of Future Obligations [§ 8.33]**

If a spouse can prove substantial injury and wishes to have past obligations divided under section 766.70(4)(a)3., he or she will probably request an order assigning future obligations as well. Wis. Stat. § 766.70(4)(a)4. This remedy may be appropriate for a spouse who lives apart from the other spouse and intends to continue that arrangement but does not wish to obtain a divorce or legal separation. An order assigning responsibility for future obligations enables the spouses to remain married but to have separate financial obligations. Such an order may also be sought by a spouse who remains with the other spouse but who wishes to protect the property that he or she earns or holds. The reason could be the other spouse's spendthrift tendencies or substantial business obligations.

Similarly, in contemplation of an action for dissolution, a spouse may wish to protect his or her interest in marital property from obligations incurred by the other spouse. Under section 766.55(2m), the marital property that a spouse receives under a judgment of dissolution is subject to the satisfaction of family-purpose debts, even if the debts are incurred after the parties are living apart. An order determining that future obligations are the obligations of the party incurring them assures a spouse that the property he or she receives in the property division will not be subject to recovery for the unsecured obligations incurred by the other spouse during the time between the entry of the decree under section 766.70(4)(a)4. and the final dissolution judgment. The decree should require that the spouses disclose the decree to creditors. Then if a spouse fails to disclose such an order to a creditor, and the creditor obtains recovery from the property of the nonincurring spouse, the incurring spouse may be subject to sanctions for contempt of court or may have the property that he or she is awarded in a subsequent property division adjusted accordingly. Wis. Stat. § 767.61(3). An action under section 766.70(4)(a)4. must be commenced before an action for dissolution is filed. Wis. Stat. § 767.331.

## **6. Classification of Property to Be Acquired in the Future [§ 8.34]**

Section 766.70(4)(a)5. provides that a court can classify property to be received after the entry of the order as the individual property of the

acquiring spouse. It is likely that a spouse wishing to assign responsibility for future and perhaps past obligations will also wish to have property to be acquired in the future classified. Debt satisfaction is based on personal liability and property classifications, and both should usually be considered in determining relief. A spouse who is separated but does not wish to obtain a dissolution, or a spouse who contemplates an action for dissolution, is most likely to seek this relief. The effect is to protect the property that each spouse earns or acquires from family-purpose obligations incurred by the other spouse during a period of separation. Each spouse is obligated by the good-faith duty to disclose the decree to future creditors, since without such disclosure those creditors are not bound by classifications set forth in the decree that adversely affect the creditors' right of recovery. Wis. Stat. § 766.55(4m).

## **7. Exceptions to Availability of Remedies [§ 8.35]**

Remedies available under section 766.70(4) are subject to exceptions. First, limitation of management and control under section 766.70(4) is not available in connection with certain business interests listed in subsections 766.70(3)(a) and (b) (i.e., a spouse's interest in a partnership, joint venture, professional corporation, or other professional association described in subsections (a) and (b)). Consequently, the nontitled spouse cannot use section 766.70(4) to obtain control of a marital property business interest described in subsection 766.70(3)(a) or (b), even if the business is being substantially injured as a result of gross mismanagement by the other spouse. Other remedies, such as for breach of the good-faith duty, may be available in such cases. If the managing spouse is not legally incompetent, a guardian cannot be appointed.

The remedies in section 766.70(4) are not available in connection with a spouse's interest in closely held corporate stock. Wis. Stat. § 766.70(3)(d). The remedies in section 766.70(4) are unavailable, regardless of whether the holding spouse is an employee of the closely held corporation. The remedies in section 766.70(4) are available, however, with respect to a marital property interest in a sole proprietorship or a limited liability company.

The remedies under section 766.70(4) are also not available for any other property in which a third party's rights would be adversely affected. Wis. Stat. § 766.70(3)(e).

### **G. Marital Property Used to Satisfy Obligations Not Within the Duty of Support or Family Purpose Doctrine [§ 8.36]**

No right of contribution or reimbursement between spouses is available for family-purpose obligations paid with marital property. However, a creditor may reach marital property to satisfy an obligation that was not incurred in the interest of the marriage or the family. These obligations include those incurred before marriage, those incurred before January 1, 1986, torts, and nonfamily purpose obligations. Wis. Stat. § 766.55(2)(c)–(d). In addition, a spouse may voluntarily use marital property under his or her control to pay such an obligation. For example, if the obligation arose before marriage, the spouse may pay with marital property, or if no voluntary payment is made, a creditor may choose to levy upon marital property (usually the obligated spouse's wages) that would have been available had the marriage not taken place. Wis. Stat. § 766.55(2)(c). Although the nonobligated spouse has a marital property interest in the obligated spouse's wages, a creditor's right to recover the obligation is not diminished by the nonobligated spouse's interest. The premarriage creditor may levy upon the marital property without first attempting to recover from the obligated spouse's nonmarital property. Under section 766.70(5), however, the nonobligated spouse then may have a right to reimbursement: he or she may recover as individual property marital property of an amount equal in value to the marital property recovered or used to meet such obligations of the other spouse.

In the context of property division in divorce, California has allowed recovery by one spouse if the other spouse has used community property to pay noncommunity debts. For example, in *Lister v. Lister*, 199 Cal. Rptr. 321 (Ct. App. 1984), the husband mortgaged the community property homestead to pay his premarital debts to his brother. He did not advise his wife of the purpose of the mortgage. Despite the fact that under California law the community was obligated to pay the husband's premarital debts, the court found that this encumbrance and payment constituted bad faith on the husband's part and justified a compensatory judgment for the wife. On the other hand, the court in *Smaltz v. Smaltz*, 147 Cal. Rptr. 154 (Ct. App. 1978), held that the husband was not required to reimburse the community for support payments made to his former spouse with community property funds, which were the only funds he had at his disposal. The court found that reimbursement is an equitable determination and that these payments neither constituted bad

faith nor were an abuse of the husband's management and control of community property.

A spouse who fails to assert a right under section 766.70(5) suffers economic loss. Assume that an obligation is incurred by a spouse during the marriage, but not for a family purpose. *See supra* ch. 5. Such an obligation is satisfied first from the nonmarital property of the incurring spouse and then from that spouse's interest in marital property, in that order. Wis. Stat. § 766.55(2)(d). Even though the creditor may reach only the incurring spouse's one-half interest in marital property, the amount not subject to recovery (the other spouse's one-half interest) continues to be marital property. If the nonobligated spouse does not exercise his or her remedy under section 766.70(5), the obligated spouse has the entire benefit of the property used to satisfy the obligation and continues to have a one-half interest in all remaining marital property. The analysis is the same for tort obligations paid with or recovered from marital property. *See* Wis. Stat. § 766.55(2)(cm).

If a spouse in obtaining an extension of credit signs a statement that the obligation is or will be incurred in the interest of the marriage or the family, that statement is conclusive in determining the creditor's right to payment. Wis. Stat. § 766.55(1); *Bank One v. Reynolds*, 176 Wis. 2d 218, 500 N.W.2d 337 (Ct. App. 1993); *see supra* ch. 6. The creditor may collect from all marital property held by either spouse. However, such a statement is not conclusive as between the spouses. If the obligation is not actually incurred for a family purpose, the other spouse may recover under section 766.70(5). *See also supra* § 8.18 (breach of the good-faith duty).

An action under section 766.70(5) must be commenced not later than one year after the obligation is satisfied. Wis. Stat. § 766.70(5); *Bille v. Zuraff (In re Estate of Bille)*, 198 Wis. 2d 867, 882, 543 N.W.2d 568 (Ct. App. 1995).

A court in another community property state has held that the nonobligated spouse has an equitable lien on the remaining community property to the extent of the amount levied in satisfaction of a separate obligation. This lien is superior to the rights of other creditors in the same property. *See deElche v. Jacobsen*, 622 P.2d 835, 840 (Wash. 1980). Whether or not such a superior lien exists in Wisconsin might sometime be the subject of legislation or judicial interpretation. If a lien

exists, it would apparently expire after the limitation period passes without commencement of an action.

It is not clear how the granting of a security interest in marital property for an obligation that is other than for support or a family purpose relates to the other spouse's right of recovery under section 766.70(5). If a spouse has management and control of marital property and can grant a security interest, the rights of the creditor in the collateral are protected. Wis. Stat. § 766.55(6). The statute of limitation applicable to a spouse's right of reimbursement begins to run when an obligation is "satisfied," and the granting of a security interest does not constitute satisfaction of an obligation. Wis. Stat. § 766.70(5). Satisfaction does not occur until the creditor is paid or the security interest is enforced and the collateral is liquidated. However, the granting of a security interest may diminish the value of an asset to the extent that there is a breach of the good-faith duty. *See* Wis. Stat. § 766.70(1); *see supra* § 8.18.

The spouse's right to reimbursement under section 766.70(5) is subject to the rights of third parties who relied on the "availability" of marital property for satisfaction of a support or family-purpose debt. Wis. Stat. § 766.70(5). A creditor whose rights arose before the entry of the order under section 766.70(5) is protected by section 766.55(4m) from the adverse provisions in the order (i.e., reclassification of marital property or recovery of nonmarital property of the incurring spouse as the individual property of the nonincurring spouse). *See infra* § 8.42. However, unless a particular asset is pledged as security for a loan, in which case the lien remains on the property even though it is transferred to the nonincurring spouse, it is unlikely that a creditor will be able to prove reliance on a particular asset to grant credit. *See* Wis. Stat. § 766.55(6). Possible proof of such reliance might be the listing of an asset as marital property on a credit application on which the creditor relied.

Finally, section 766.70(5) specifically provides that a court may invoke equitable considerations. For example, a spouse may be obligated to support dependents from a prior marriage, an obligation that qualifies under section 766.55(2)(c)1. as one arising before the subsequent marriage. This debt may be satisfied from the part of marital property that would have been available but for the subsequent marriage, which would include the marital property interest of the subsequent spouse in the property so used. The subsequent spouse would then be



entitled to bring an action for reimbursement. However, under equitable principles, it might not be fair to order that an amount equal to each support payment made in the past or to be made in the future be set aside as the subsequent spouse's individual property, particularly if the spouses are unable to accumulate significant amounts of marital property. *See Smaltz v. Smaltz*, 147 Cal. Rptr. 154 (Ct. App. 1978). On the other hand, such reimbursement may be fair if the payor spouse has substantial individual property available for use as payment but chooses to use his or her earned income or other marital property. *See In re Lam*, 364 B.R. 379 (Bankr. N.D. Cal. 2007) (husband paid child support from prior marriage with community property when he had separate property available; bankruptcy court excepted from discharge resulting obligation imposed by divorce court, on ground of husband's defalcation in a fiduciary capacity under California law).

If a spouse's salary or wages are used to pay an obligation that arose during the marriage but before the effective date of the Act and that would have been a family-purpose obligation under the Act, it seems inequitable to allow recovery under this subsection. The same reasoning applies if a nontortfeasor's interest in marital property is used to pay a tort obligation that would be within the family-purpose obligation if the doctrine were applied to torts. Reference to cases in community property states that follow the family-purpose doctrine for torts may be helpful. *See supra* § 6.9.

Section 766.70(5) refers to reimbursement from marital property. It would be logical to infer that a court could require that the defendant spouse transfer nonmarital as well as marital property to the other spouse as reimbursement for marital property used by the defendant spouse for other than a family-purpose obligation. There is nothing in the Act that would as a matter of policy prevent this result. If such a transfer is ordered, one-half the value of the marital property wrongfully transferred (the value of the recovering spouse's one-half interest) would be paid from the nonmarital property of the defendant as reimbursement of the interest of the recovering spouse. *See also infra* § 8.38 (regarding damages).

## H. Special Issues [§ 8.37]

### 1. Damages [§ 8.38]

When one spouse is able to show a right to recover from the other spouse under section 766.70, the measure of damages, including punitive damages under appropriate circumstances, depends on the factual and equitable circumstances of each case. For example, in *Brooks v. Brooks*, 612 S.W.2d 233 (Tex. Civ. App. 1981), a community property case involving a request for reimbursement of the husband's separate property from the community, the husband was able to trace how much was paid out of the corpus of his separate-property corporation during the marriage for the benefit of the community. His measure of recovery was the amount expended from the corpus of the corporation. The court held that it was not necessary to show the value of the benefit to the community, even if it differed from the amount expended. Absent an agreement to the contrary in Wisconsin, the use of individual property for family purposes probably results in the reclassification of that property as marital property, but *Brooks* may be helpful in determining how damages are measured in an appropriate case. See Wis. Stat. § 766.63 (mixed property); see also *Penick v. Penick*, 783 S.W.2d 194 (Tex. 1988) (discussion of equitable considerations in reimbursement).

On the other hand, the wife in *Logan v. Barge*, 568 S.W.2d 863 (Tex. Civ. App. 1978), could not prove the dollar amount of community property expended by her deceased husband in concert with his daughter, son, and daughter-in-law in acquiring a business and other property in the names of the latter three persons. The court held that the proper measure of damages was the enhanced value of the property in the hands of the recipients, not the dollar amount transferred, citing *Burton v. Bell*, 380 S.W.2d 561 (Tex. 1964), but the evidence produced at trial was inadequate to support the jury's verdict. See also *Swope v. Swope*, 739 P.2d 273, 282–83 (Idaho 1987) (holding that measure of damages to community is enhanced value of spouse's separate property because of community property earnings used to increase value of separate property).

In *Auger v. Auger*, 381 So. 2d 879 (La. Ct. App. 1980), the court allowed recovery from a husband who, in anticipation of a divorce, transferred property without consideration to his relatives and business associates. His purpose was to reduce his wife's community property

interest in assets divided incident to the divorce. The court found that the wife was entitled to judgment against him in the amount of one-half the fair-market value of the transferred properties.

Similarly, in *Hall v. Allred*, 385 So. 2d 593 (La. Ct. App. 1980), the former husband sold property that had appreciated in value to his uncle, the previous owner of the property, for the same amount that the former husband had paid for the property approximately six years earlier. The former wife sued both men. The court held that the former husband had intentionally deprived her of her interest in community property and found that the measure of damages was one-half the difference between the property's fair market value when purchased in 1971 and when reconveyed in 1977. The court cited *Thigpen v. Thigpen*, 91 So. 2d 12 (La. 1956), as authority (awarding wife damages equal to one-half of difference between fair-market price and consideration received). *But see Fowler v. Fowler*, 861 So. 2d 181 (La. 2003) (holding, under Louisiana law, that life-insurance proceeds are separate property of beneficiary, regardless of source of premiums, and overruling *Thigpen* on life-insurance issue).

One court made the distinction between recovery sought incident to a dissolution action, which could be analogous to a Wisconsin interspousal remedy, and recovery sought after the death of the donor. *Osuna v. Quintana*, 993 S.W.2d 201, 209 (Tex. App. 1999). In that case, the husband conveyed substantial gifts of community property to another woman. In awarding judgment for joint-and-several liability against both the other woman and the husband for the full value of community property transferred, the court noted the difference in appropriate damages after the death of a spouse or while both spouses were alive but involved in a divorce. It pointed out that at death a party has the right to convey one-half the community property to whomever he or she wishes. Therefore, only one-half of community property is subject to recovery for improper transfers of community property. However, at divorce, all community property, including community property that was wrongfully transferred, is subject to division. Consequently, the court imposed a resulting trust, and required that the entire property transferred be returned to the community.

All the foregoing cases involved money damages. Under certain circumstances (e.g., the transfer of a unique asset such as an art object or real estate that is classified as marital property), rescission of the transfer or other remedy might be appropriate.

Section 766.70(6)(a) enables a nonparticipating spouse to sue either the spouse making the gift of marital property, the donee, or both, if the gift exceeds the value limits set by section 766.53. It is not clear how the Act would treat a bargain sale—in other words, part sale and part gift, as occurred in *Hall*. It appears that a spouse encountering such a fact situation could sue the grantee, and the court could order return of the property. The return should, of course, be conditioned on return of the consideration paid by the grantee. If the grantor spouse were unable to return the consideration, it might not be equitable to rescind the transfer. The relationship between the grantor and the grantee would probably enter into the court's consideration of these alternative remedies.

Section 766.70(1), regarding breach of the good-faith duty, does not classify the recovery under that subsection. Therefore, section 766.31(7)(e), which classifies such a recovery as individual property unless a decree or marital property agreement provides otherwise, applies.

It should be noted that the measure of damages to the property interests of a spouse under section 766.70(1) would be the full amount of marital property damaged if recovery is from marital property and one-half the amount if recovery is from the liable spouse's nonmarital property.

➤ **Example.** Assume that a wife squanders \$20,000 of marital property. Therefore, the husband's undivided one-half interest in marital property (valued at \$10,000) and the wife's one-half interest (also valued at \$10,000) are gone. The husband must recover \$20,000 of former marital property as his individual property to receive a value of \$10,000 from the wife's share of the former marital property. The other \$10,000 in value in the recovery already represents the husband's interest in the former marital property that is now reclassified as his individual property.

If the damage has been to one spouse's nonmarital property and recovery is from marital property, the recovering spouse must receive twice the value of the damaged property. This is necessary to achieve a transfer of the defendant spouse's one-half interest in marital property that is equal to the value of the nonmarital property damaged.

A spouse who owns nonmarital property and who has management and control over marital property may choose the property from which a

judgment for an interspousal remedy is voluntarily paid. If the judgment is not paid voluntarily, the recovering spouse may choose the property subject to execution or garnishment. If recovery is from predetermination date property owned by the liable spouse rather than from the liable spouse's individual property, the recovering spouse may be receiving property that is potentially augmented deferred marital property and that he or she could later elect to receive if the liable spouse dies before the recovering spouse. Wis. Stat. §§ 861.018–.11. The recovering spouse has no such elective rights in the liable spouse's individual property. Consequently, the recovering spouse should consider the classification of property to be recovered.

➤ **Example.** Assume that a husband is entitled to recover \$20,000 of marital property or \$10,000 of his wife's nonmarital property as a result of her wrongful transfer of \$20,000 of marital property. The wife has a solely owned bank account with a \$10,000 balance consisting of predetermination date property that would constitute augmented deferred marital property at her death. She also has an individual property account that contains \$10,000. Further assume that the wife continues to hold these accounts and dies before her husband. If the husband recovers for the interspousal remedy the \$10,000 in the account holding individual property, he may elect under section 861.02 to receive an additional \$5,000 from his wife's predetermination date account in her estate. If the husband recovers the interspousal judgment from the wife's predetermination date account, he will lose the potential right to elect to receive one-half of this account upon the wife's death.

If the bank account that is the wife's individual property was acquired by gift or inheritance, it would not usually be subject to division at divorce. Wis. Stat. § 767.61. However, an account holding property that potentially may become part of the deferred augmented marital property to which the other spouse has a right or an account holding property brought to the marriage is subject to division at divorce. The husband may wish to recover from the individual property account holding inherited funds rather than from the account holding other nonmarital funds to preserve the possibility of further recovery from the wife's assets if the marriage is dissolved or if the wife dies before the marriage is dissolved. *See infra* ch. 11, ch. 12; *see also supra* § 6.110 (dischargeability in bankruptcy of claims between spouses).

## 2. Exemptions [§ 8.39]

It is not clear what effect, if any, the exemptions under section 815.18 have on a judgment in favor of one spouse against another. For example, a third-party creditor with a judgment against a spouse cannot recover a depository account of up to \$5,000 from the debtor. Wis. Stat. § 815.18(3)(k). Married debtors may each claim an exemption in the same property, thereby doubling the value and exempting up to \$10,000. Wis. Stat. § 815.18(8). However, assume that a wife obtains a judgment against her husband for \$5,000, and that the recovery is classified as the wife's individual property. The wife must recover \$10,000 of marital property or \$5,000 of the husband's nonmarital property to satisfy the judgment. *See supra* § 8.38. If the husband holds a marital property bank account of \$10,000, does the wife recover the entire amount as individual property? Or may she only recover \$5,000, because the husband holds \$5,000 as exempt property? *See* Wis. Stat. § 815.18(3)(k). If he continues to hold \$5,000 as exempt under section 815.18(3)(k), is it still marital property? Judicial interpretation or clarifying legislation is needed to resolve these issues.

## 3. Access to Employee's Wages by Nonemployee Spouse [§ 8.40]

Earnings from employment represent the largest marital property asset for most couples. Section 109.01(3) defines *wages*, in part, as "remuneration payable to an employee for personal services." Section 109.03(1) states that "[e]very employer shall as often as monthly pay to every employee ... all wages earned by the employee." Payment to any person other than the one actually performing the services would therefore require specific authorization by statute, as in the case of court-ordered payment of support of dependents under section 767.225(1)(c). No such specific authorization exists in the Act, and it appears that the general remedies under section 766.70(2) and (3) are limited by the specific statutes relating to payment of employees.

If only the employee is paid by the employer, as is required by section 109.03(1), then only that employee spouse has management and control over the cash wages or paycheck. *See supra* § 4.18; *see also* Wis. Stat. § 766.51(1)(am). To divest a spouse of control over marital property otherwise within his or her management and control requires a showing

of actual or potential damage to marital property by gross mismanagement, waste, or absence. Wis. Stat. § 766.70(4)(a). Therefore, it appears that access and add-a-name remedies under section 766.70(2) and (3), which require no wrongdoing but arise solely by reason of ownership, are not available to require placement of both names on a spouse's paycheck or the issuance of two checks by the employer. On proof of gross mismanagement, waste, or absence, it appears that the court could order temporary or permanent limitation of the employee's management and control of his or her wages. Wis. Stat. § 766.70(4)(a)1.

Protection of the nonmanaging spouse's marital property right in his or her spouse's wages is often most crucial when a dissolution action is pending. Protection could be provided by a temporary order requiring that paychecks be issued in both names or that two checks be drawn, one for each spouse. However, this does not appear to be among the forms of temporary relief available incident to the dissolution action. Section 767.75 provides for direct payment of income to the court for temporary child support, maintenance, family support, spousal support, certain costs, and attorney fees. Property division or access to property under section 766.70 is not mentioned in section 767.75, and therefore, a temporary order for direct payment is not authorized. Moreover, no authority is granted to the court under section 767.225(1) to order the division of wages as a form of property division, although the amount of support ordered by the family court commissioner can accomplish the same result.

Because division of wages according to the property interests of each spouse, if the remedy is available, cannot be made incident to the dissolution action as a temporary order, it must be authorized, if at all, under section 766.70. However, an action under section 766.70 must be commenced before the commencement of the dissolution action. Wis. Stat. § 767.331. Once the dissolution action is pending, an interspousal remedy cannot be commenced. *Id.* There would be no sound policy reason to allow adding a name to a paycheck if a section 766.70(3) action was commenced before the dissolution action and not to allow such a remedy if the dissolution was filed first. It therefore appears that such a remedy might not be appropriate in either instance.

Other statutes indicate that it is the policy of Wisconsin to restrict the assignment of income, even by one who earns it. For example, wage assignments associated with consumer transactions must be revocable at

will and are limited in time. Wis. Stat. § 422.404. Wage assignments without a spouse's consent are invalid as fraudulent contracts except in limited situations. Wis. Stat. § 241.09.

It is arguable that the right to receive future earned income, even though subject to the contingency of future employment, is an interest vital to the concept of marital property. *See supra* § 5.22. Nevertheless, almost all the remedies set forth in section 766.70 relate to property, obligations, or rights in existence at the time of the commencement of the action, not those that are to be acquired in the future. The two exceptions, in subdivisions 766.70(4)(a)4. and 5., permit the court to classify future obligations and acquisitions of property and to order that any obligation or property acquired by a spouse is the obligation or the individual property of the incurring or acquiring spouse. Neither of these remedies provides a spouse with access to the marital property paycheck of the other spouse.

In summary, it appears that none of the remedies under section 766.70 is available to provide direct access by the nonemployee spouse to the employee's wages. Whether or not remedies under the Act supersede chapter 109 and other statutes to the contrary may be clarified by subsequent legislation or by judicial interpretation.

#### **4. Guarantees [§ 8.41]**

In determining the availability of assets to the creditor, a guarantee executed before the determination date and enforced thereafter is treated as an obligation in existence on the determination date. Wis. Stat. § 766.55(3). The spouse of the guarantor may, subject to equitable considerations, have a right of reimbursement under section 766.70(5) for marital property used to pay such an obligation. *See supra* § 8.36. The damage occurs at the time of payment, and the applicable statute of limitation runs from payment, not execution, of the guarantee.

The execution of a guarantee by a spouse after the determination date is not ordinarily an event causing damage to marital property. Without damage, the cause of action under section 766.70 does not arise and the statute of limitation does not run. The subsequent payment of the obligation with marital property may give rise to a remedy on behalf of the spouse who did not join in the guarantee. Wis. Stat. § 766.70(5), (6)(a).



Whether the obligation under a guarantee is a family-purpose obligation determines the classifications of property available to the creditor. *See* Wis. Stat. § 766.55(2)(b), (d). If a marital-purpose statement is signed by the incurring spouse, it is conclusive evidence as to the creditor that the guarantee is a family-purpose obligation. Wis. Stat. § 766.55(1); *Bank One v. Reynolds*, 176 Wis. 2d 218, 220–21, 500 N.W.2d 337 (Ct. App. 1993). A general analysis of other types of family-purpose obligations may be helpful. *See, e.g., supra* ch. 5, ch. 6. For example, a personal guarantee of an obligation of a family-owned corporation might be for a family purpose, but the guarantee of a loan to someone who is not a family member without benefit to the family might not be.

The Act does not provide for contribution between spouses for family-purpose obligations, so a guarantee of such an obligation does not give rise to a remedy. Payment of a nonfamily-purpose guarantee with marital property, however, may support a remedy under section 766.70(5), which permits reimbursement for a nonfamily-purpose obligation satisfied with marital property. *See supra* § 8.36. A remedy may also be available under section 766.70(6)(a) for reimbursement of the amount paid in excess of the gift limits in section 766.53. *See infra* § 8.45.

There may be instances in which the execution, not the enforcement, of a guarantee results in damage to marital property. For example, the existence of the guarantee may make the acquisition of other credit unavailable. If the execution of the guarantee is for a purpose that supports an action for breach of the good-faith duty, and if damage to the other spouse's property can be proved, then the nonguarantor spouse may have a remedy under section 766.70(1). *See supra* § 8.18; *see also supra* § 6.22; *infra* § 8.66 (complaint form).

## **5. Effect of Decree on Subsequent Creditors [§ 8.42]**

Section 766.55(4m) provides that a court decree under section 766.70 (or marital property agreement or unilateral statement under section 766.59) does not adversely affect a creditor's rights unless the creditor had actual knowledge of the adverse provisions in the decree when the obligation was incurred. If a creditor is provided a copy of a decree under section 766.70 before an obligation is incurred, the creditor is bound by any adverse provisions, regardless of whether the creditor read

or understood its provisions. Wis. Stat. §§ 766.56(2)(c), .59(5); *see supra* § 6.81. In the case of an open-end credit plan (e.g., a credit card), *see* Wis. Stat. § 766.555(1)(a), the creditor must have actual knowledge or a copy of the decree when the plan is entered into. Wis. Stat. §§ 766.55(4m) (actual knowledge), .56(2)(c) (copy). If the actual knowledge or disclosure occurs after the obligation is incurred or the plan is entered into, then the decree will not affect the creditor's rights with respect to any subsequent use of the plan or any renewal, extension, or modification of the obligation. Wis. Stat. §§ 766.55(4m), .56(2)(c). The creditor may recover the amount owed from marital property classified as such by law, rather than by the decree, as if the decree did not exist.

Any creditor in a credit transaction governed by chapters 421 to 427 (the Wisconsin Consumer Act) must provide notice on the application that no provision of a marital property agreement, unilateral statement under section 766.59, or court decree concerning an interspousal remedy under section 766.70 is binding on the creditor unless the creditor is provided a copy of the relevant document or has actual knowledge of any adverse provision before or when the obligation is incurred. Wis. Stat. § 766.56(2)(b). The applicant decides whether to provide a copy of the agreement or to provide the creditor with actual knowledge of an adverse provision by other means. If the applicant does not do so, the creditor is not bound and may rely on and collect from property that would have been marital property and that would have been available for recovery by the creditor without the agreement, notice, or decree.

A spouse whose property is recovered by a creditor of the other spouse because the creditor had no notice or knowledge of the decree, or a spouse whose property is used by the other spouse to pay such a creditor in contravention of the provisions of a decree under section 766.70, may have a remedy against the other spouse for breach of the good-faith duty under section 766.70(1). *See also infra* § 8.18. Decrees under section 766.70 should include a provision requiring each spouse to disclose the decree and to provide a copy of the decree to potential creditors. Such a requirement should also make a contempt remedy available if the order is violated. *See* Wis. Stat. §§ 785.01(1)(b), .02.

## **6. Effect of Decree on Bona Fide Purchaser [§ 8.43]**

Section 766.57(3) provides that a bona fide purchaser who buys property from a spouse who has the right to manage and control property takes the property free of claims of the other spouse. *Bona fide purchaser* is defined in section 766.57(1) as a purchaser without notice of a spouse's adverse claim. It appears that a purchaser with no actual notice of a decree issued under section 766.70 takes the property free of the decree's provisions. *See also* Wis. Stat. § 766.70(8); *supra* § 4.66.

## **IV. Actions by Spouse Against Third Parties and Other Spouse [§ 8.44]**

### **A. Recipient of Gift of Marital Property in Excess of Value Limit [§ 8.45]**

A spouse acting alone may make gifts to a third person of marital property over which the donor spouse has management and control. *See* Wis. Stat. § 766.51(4). Such a transfer results in a completed gift, subject to the other spouse's exercise of his or her remedy to recover the gift or to obtain a compensatory judgment for the amount by which the gift exceeds the applicable limit. If aggregated gifts to any one donee in one calendar year exceed \$1,000 or exceed an amount that is reasonable considering the economic position of the spouses, then the nondonor spouse may have such a remedy. *See* Wis. Stat. §§ 766.53, .70(6)(a), .51(4); *see also supra* ch. 4, *infra* ch. 12.

A transfer of marital property to a revocable trust created by the donor spouse or a deposit into a joint or payable-on-death (P.O.D.) account with a spouse and a third party is not a completed gift. The spouse having control generally has not relinquished that control, and the transfer or deposit would not ordinarily result in damage. However, see sections 8.47–49; *infra*, concerning such transfers upon the death of the transferring spouse. *See* section 2.102, *supra*, concerning transfers to an irrevocable trust with the donor's retained interest.

The nondonor spouse may bring an action against either the donor spouse, the recipient, or both, either to recover the gift or for a compensatory judgment equal to the amount by which the gift exceeded the limit established under section 766.53. Wis. Stat. § 766.70(6)(a). If

the gift was cash, the recovery would probably be a compensatory amount rather than the cash itself.

Whether a court will require either return of the property or a compensatory judgment against the transferor spouse or the recipient of property who paid less than fair consideration may depend on the equities in each case. *See, e.g., Hall v. Allred*, 385 So. 2d 593 (La. Ct. App. 1980). Factors to be considered may include whether the consideration received by the transferor could be returned, the relationship between the transferor and the transferee, and the property's value and nature. In most community property states, transfers of community property without consideration by one spouse without the other's consent are voidable but not void. *See Reppy & Samuel, supra* § 8.8, at 239–40; *Osuna v. Quintana*, 993 S.W.2d 201 (Tex. Ct. App. 1999); *Harris v. Harris*, 369 P.2d 481, 482 (Cal. 1962); *Novo v. Hotel Del Rio*, 295 P.2d 576 (Cal. Ct. App. 1956).

Questions have been raised concerning gifts of marital property that financially assist relatives to whom a spouse has no legal duty of support. The nonparticipating spouse's right to recover these gifts is uncertain. *See supra* § 4.36. The recipients of these gifts typically are college-age children and elderly parents. It is possible for a spouse to become legally obligated to support children after the age of majority when the spouse agrees to do so incident to a divorce settlement, *see, e.g., Bliwas v. Bliwas*, 47 Wis. 2d 635, 178 N.W.2d 35 (1970); *Honore v. Honore*, 149 Wis. 2d 512, 439 N.W.2d 827 (Ct. App. 1989), but usually this financial assistance is gratuitous. Section 766.70 states only that a spouse may bring an action for recovery of gifts of marital property in which he or she did not act with the donor spouse; it does not mandate that the court order recovery from the donor spouse if such a gift is proved. The fact that the court *may* order recovery implies that equitable considerations may apply. The amount of the gift in relation to the spouses' economic circumstances, the availability of the donor's nonmarital property, and the relationship between the donor and donee, for example, may be relevant to the court's decision. *See also In re Lam*, 364 B.R. 379 (Bankr. N.D. Cal. 2007) (divorce court had found debtor husband liable for using community property to pay child support from prior marriage when separate property had been available).

Section 766.70(6)(a), which provides the remedy for recovery of unauthorized gifts of marital property, states that “[i]f the recovery occurs during marriage, it is marital property. If the recovery occurs

after a dissolution or the death of either spouse, it is limited to 50% of the recovery that would have been available if the recovery had occurred during the marriage.” If the property is recovered during marriage either from the donee or from the donor spouse who has sufficient nonmarital property with which to satisfy the judgment, the recovery is marital property. Wis. Stat. § 766.70(6)(a). The effect of the recovery is to replace the marital property that was given away. It appears, however, that property recovered from the donor spouse during the marriage should be the individual property of the nondonor spouse if the donor has no nonmarital property and must satisfy the judgment out of his or her share of marital property. Otherwise, the nondonor spouse has recovered nothing. Twice as much marital property would be necessary to satisfy the judgment as would be necessary if satisfied by the donor’s nonmarital property. *See supra* § 8.38. This apparent oversight might be addressed by subsequent legislation.

The action for recovery of a gift of marital property must be commenced within one year after the nondonor spouse has notice of the gift, within one year after dissolution, or within the time limit for filing claims after the death of either spouse, whichever is earliest. Wis. Stat. § 766.70(6)(a). When the nondonor spouse dies, his or her personal representative must bring the action within the time for filing claims under section 859.01. There are no provisions for extending this time.

This remedy applies only to gifts of marital property, not to gifts of predetermination date property, even if the predetermination date property would have been marital property if the Act had been in effect when the property was acquired. If recovery of predetermination date property is sought after the death of the donor, section 861.17 (transfers in fraud of a spouse’s rights) may apply in unusual circumstances, or sections 861.018 through .11 (election of the augmented deferred marital property estate, including certain transfers in which the donor has retained an interest or control) may apply.

## **B. Recipient of Gift by Nonprobate Transfer at Death of Spouse [§ 8.46]**

### **1. Multiple-party Bank Accounts; P.O.D. Arrangements; Dispositive Revocable Trusts [§ 8.47]**

#### **a. Transferor Dies First [§ 8.48]**

Occasionally, one spouse is a party on a joint account, such as a bank account or similar depository account, with a person other than his or her spouse. Assuming the spouse is the only depositor, there is no gift when the arrangement is made, but the arrangement results in a completed gift when withdrawals are made by the nondepositor during the donor spouse's lifetime or at the death of the spouse who provided the funds in the account. Upon the death of the spouse who is a party, the entire balance passes to the surviving third party. *See* Wis. Stat. § 705.04. If any of the funds deposited by the decedent were marital property, the surviving spouse may recover from the other party one-half of the funds determined to be marital property. Wis. Stat. §§ 766.70(6)(b), 705.04(4).

The issue of a surviving spouse's interest in a multiple-party account held by the decedent spouse arose in *Lloyd v. Lloyd (In re Estate of Lloyd)*, 170 Wis. 2d 240, 487 N.W.2d 647 (Ct. App. 1992). The court of appeals held that certain of the joint bank accounts held by the decedent and his nephew and other third parties were funded with marital property and were subject to recovery under section 766.70(6) by the decedent's surviving spouse. *See also* Wis. Stat. § 705.04(4). The circuit court had held that most of the accounts were entirely funded with marital property because there was insufficient tracing to find otherwise. The circuit court's determination of tracing and commingling were questions of fact, but whether those funds were classified as marital or nonmarital property were questions of law that the court of appeals reviewed *de novo*. *Lloyd*, 170 Wis. 2d at 251–52. The court of appeals reviewed the evidence and held that some of the joint accounts were funded with the decedent's solely owned or predetermination date funds. The court stated that even though the surviving party to an account is presumptively the owner, interest earned on the account and “unexplained” funds added to the account between the date of the marriage and the determination date are deferred marital property, and funds added between the determination

date and date of death are marital property. *Id.* at 266. See also the discussion of deferred marital property elections in chapter 12, *infra*. At least one multiple-party account was funded before the marriage and placed in the names of the decedent and his nephew before the effective date of section 861.05. This account was thus excluded from the augmented estate by section 861.05(4), and the surviving spouse had no right to recover the portion of that account that was traceable to the decedent's nonmarital property. *Lloyd*, 170 Wis. 2d at 266. It was apparently conceded that all the funds deposited to the accounts in question were deposited by the decedent and not by other parties to the accounts.

Section 766.70(6)(b) applies only to deposits made to multiple-party accounts or to other incomplete transfers after the determination date. *See* Wis. Stat. Ann. § 766.70 Legis. Council Notes—1985 Act 37, §§ 89, 130 to 138 (West 2009). Any deposits to such accounts before the determination date that would have been marital property had the Act been in effect are predetermination date property. A surviving spouse's right in such property arises only at the death of the owner spouse and is governed by the surviving spouse's election of the augmented marital property estate. *See* Wis. Stat. § 861.03. If interest is posted to the account after the determination date and may therefore be marital property (if no unilateral statement under section 766.59 has been executed), then the amount attributable to deposits made by the decedent spouse, but not to deposits made by the third party, is subject to the surviving spouse's remedies under section 766.70(6)(b).

If an account is payable at the death of the owner to a designated third party, the surviving spouse has a similar right to recover from the P.O.D. beneficiary one-half the deposits that are marital property and that were made after the determination date. A financial institution is protected upon payment of funds to the surviving individuals who are, according to the institution's records, entitled to such funds at the death of a party. *See* Wis. Stat. § 705.06.

If a spouse acting alone creates a revocable trust during marriage, and marital property is transferred to the trust, there is no completed transfer to a third party. The transfer to the trust "by itself" does not cause property to be reclassified. Wis. Stat. § 766.31(5); *see supra* § 2.101. The trust may, by its terms, become irrevocable at the death of the settlor spouse. If someone other than the spouse of the settlor has an interest in the trust that arises at the settlor's death, and distributions are made to

that person, then the surviving spouse may recover one-half of the former marital property from the recipient who was the trust beneficiary.

If former marital property continues to be held by the trustee after the settlor dies, then the surviving spouse's action under section 766.70(6)(b) is against the trustee to recover his or her one-half interest in the former marital property so held. The 1988 Trailer Bill created section 766.575 to protect a trustee of a trust established by one spouse when the trustee has no knowledge of an adverse claim of the nonsettlor spouse. Section 766.575(3) also establishes the procedure to follow if the trustee receives notice of a claim. The trustee is required to suspend distribution for 14 business days and provide to the trust beneficiaries notice of the claim. Wis. Stat. § 766.575(3)(a). The claimant spouse must provide certain documentation to support the claim within those 14 days, and if such support is provided, the trustee is required to suspend distributions until the claim is resolved. Wis. Stat. § 766.575(3)(b). If the claimant spouse does not provide required documentation supporting the claim, the trustee may administer the trust as if no claim had been asserted. Wis. Stat. § 766.575(3)(c); *see also supra* § 2.100.

The concept of allowing recovery by the surviving spouse of one-half the value of the nonprobate transfer (not the transferred property itself) is consistent with the decedent's ability to manage the property. Thus, a spouse with management and control of marital property can establish an arrangement that will transfer marital property at the spouse's death to a third person, but such a transfer is subject to the other spouse's remedy for one-half the value. The remedy is stated in terms of "value" because the nondonor spouse is divested of the property itself by the arrangement.

An action to recover a nonprobate transfer taking effect at death must be commenced by the surviving spouse no later than one year after the death of the decedent spouse who made the arrangement. Wis. Stat. § 766.70(6)(b)1.; *see Joyce v. Joyce (In re Estate of Joyce)*, 2008 WI App 92, 312 Wis. 2d 745, 754 N.W.2d 515 (review denied).

## **b. Nontransferor Dies First [§ 8.49]**

If the spouse entitled to recover predeceases the transferor, section 766.70(6)(b)2. applies. It appears that the action must be brought no later than one year after the nontransferor's death, although the statute is unclear as to which spouse's death determines when the one year begins



to run. It is logical that the time should begin to run at the death of the spouse having a claim. The marital property that is subject to the arrangement made for a third party is still held by or under the control of the surviving donor spouse, because this remedy applies only to transfers taking effect at the death of the donor. A completed transfer has not taken place because the spouse making the arrangement has not yet died. Because it is due on demand, marital property in a multiple-party account or revocable trust should be treated like any other marital property controlled by the surviving spouse. The nondonor decedent's share of the marital property must be recovered by his or her personal representative, who will administer the property as part of the nondonor's estate. *See, e.g., Bolton v. MacDonald (In re Estate of MacDonald)*, 794 P.2d 911 (Cal. 1990) (holding that estate could recover community property interest in individual retirement accounts (IRAs) held by surviving spouse, because decedent had consented only to designation of trust as beneficiary but did not consent to transmutation of her interest).

An additional provision of section 766.70(6)(b)2. states that recovery is limited to the value of the property at the date of death of the recovering spouse, not at the subsequent death of the surviving donor spouse (when the transfer actually takes place). Therefore, it appears that the recovering nontransferor spouse's estate is not entitled to any increase in the value of the property after the nontransferor's date of death. This is not entirely consistent with the concept of marital property assets in a revocable trust or multiple-party account, although it may be logical with respect to life insurance insuring the life of the survivor.

➤ **Example.** A husband creates a revocable trust holding marital property stock and makes his son from a previous marriage the beneficiary. His wife dies on a date when the stock is worth \$10,000. Six months later, the stock is worth \$50,000. It appears that the wife's estate is entitled to recover only \$5,000 from the husband or his trust, that is, one-half the value on the wife's date of death, even though the husband is still alive and no transfer has taken place. If the husband had not transferred the stock to the trust, the wife's estate would have owned one-half of the stock itself. If the wife's personal representative fails to bring an action to recover marital property controlled by the husband within the one-year limitation, then the wife's heirs or estate cannot later claim an interest in the transferred property after the husband's death. Wis. Stat. § 766.70(6)(b)2.

There may be instances in which the spouse who made the arrangement resulting in a nonprobate transfer at death dies after the death of the spouse entitled to a remedy but before the recovering spouse's personal representative can exercise the remedy. The recovery is the same as if the donor had predeceased the recovering spouse, but the recovery is valued as of the recovering spouse's date of death. Wis. Stat. § 766.70(6)(b)2.

The remedy in section 766.70(6)(b) is consistent with the principle that a spouse may not, by nontestamentary disposition, divest the other spouse of his or her interest in the value of marital property (although the property itself may be divested). *Denoskoff v. Scott (In re Estate of Politoff)*, 674 P.2d 687 (Wash. Ct. App. 1984), illustrates this rule. When the wife died, the husband had approximately \$32,000 in community funds in his sole name. He deposited these funds in a joint bank account with his housekeeper. When he died, the housekeeper received the money as the surviving joint tenant. The wife's heirs recovered the wife's share of the community funds from the housekeeper on the ground that the husband could not divest the wife (or in this case, her estate) of her interest in community property assets by placing them in a joint account with a third person.

## **2. Beneficiary of Life Insurance Policy Insuring Life of a Spouse [§ 8.50]**

### **a. Insured Dies First [§ 8.51]**

Another type of arrangement that transfers property at the death of a spouse is the beneficiary designation on a policy insuring the life of a spouse. The surviving spouse may have a marital property interest in the policy or proceeds. *See supra* ch. 2. The noninsured spouse may also have a marital property interest in a policy owned by a third party and insuring the life of a spouse if the premiums were paid with marital property. Wis. Stat. § 766.61(3)(d); *see supra* §§ 2.158–.183. If someone other than the spouse of the insured is the beneficiary of more than one-half the proceeds classified as marital property, the surviving spouse may recover his or her marital property interest in the proceeds from the beneficiary. Wis. Stat. § 766.70(6)(b)1.; *see also Roselli v. Rio Cmty. Serv. Station, Inc.*, 787 P.2d 428 (N.M. 1990). If the policy is mixed property, the spouse's share is one-half the proceeds determined

to be marital property using the same fraction used to calculate the proportionate interests during the owner's lifetime. Wis. Stat. § 766.61(3); *see supra* ch. 2.

The court in *Socha v. Socha*, 204 Wis. 2d 474, 555 N.W.2d 152 (Ct. App. 1996), determined that section 766.70 was the only remedy available to the wife when her insured husband died during the pendency of their dissolution action. The husband had changed the beneficiary of marital property life insurance and retirement benefits from the wife to their son. The change was done in violation of temporary orders entered in the dissolution action. The circuit court imposed a constructive trust on the insurance proceeds, but the court of appeals held that since a cause of action for divorce terminates when a party dies, and the legislature has fashioned comprehensive remedies for transfers of marital property when no dissolution action is pending, the parties' rights had to be determined under section 766.70. The court of appeals remanded the action for such a determination.

Recovery under section 766.70(6)(b) may be barred if the surviving spouse signed a written consent to the designation of a third-party beneficiary. Wis. Stat. § 766.61(3)(e). While disclosure of assets and financial obligations may be required under section 766.58(6)(c)1. for a marital property agreement, such disclosure is not necessary to make the written consent enforceable. *See supra* § 2.208.

Any action against a beneficiary must be commenced within the limits prescribed for other transfers taking effect at death, that is, not later than one year after the insured's death. Wis. Stat. § 766.70(6)(b)1.

A life-insurance company that pays a third party without knowledge of an adverse claim by the surviving spouse is protected by section 766.61(2). If the company is aware of such a claim, the company should hold the proceeds until the rights of the surviving spouse in the proceeds are decided, or the insurer may wish to commence an interpleader action under section 803.07.

The right of recovery under section 766.70(6)(b) does not reach a policy assigned to or payable to a creditor as security for a loan. Wis. Stat. § 766.61(4). It also does not reach proceeds received by a former spouse or minor children if the decedent was required to maintain the policy by a judgment of divorce or legal separation or by a judgment in a paternity action, regardless of the fact that premiums may have been paid

with marital property during the subsequent marriage. Wis. Stat. § 766.61(5).

### **b. Noninsured Dies First [§ 8.52]**

In addition to any ownership interest in a policy insuring the life of the surviving spouse that is the decedent's nonmarital property, the estate of a deceased noninsured spouse has an ownership interest in the marital property portion of a policy insuring the life of the surviving spouse. *See* Wis. Stat. § 766.70(7). If the surviving spouse does not exercise his or her right to purchase the policy under section 766.70(7), the decedent's marital property interest in the policy passes to the heirs or beneficiaries of the estate. *See infra* § 8.59. How premiums are to be paid, who may designate beneficiaries, and how a policy can be split between owners are matters not addressed by the Act.

Obviously, the estate of the noninsured spouse has no right to recover under section 766.70(6)(b)2. from a third-party beneficiary, because the insured is still alive. However, if the insured dies before the policy is transferred to the new owner (heir or beneficiary) by the deceased noninsured spouse's estate, and a third party is the beneficiary, then the right of recovery is limited to one-half the marital property component of the policy valued on the date of death of the noninsured spouse. Wis. Stat. § 766.70(6)(b)2.

The estate of the predeceasing noninsured spouse is entitled to approximately the same amount of compensation regardless of whether the surviving spouse exercised his or her option under section 766.70(7) to purchase the policy or whether the surviving spouse died before or after having done so. Recovery from the third-party beneficiary is limited to the noninsured spouse's marital property interest in the interpolated terminal reserve of a nonterm policy, which approximates the "cash value," and the unused premium of a term policy. Wis. Stat. § 766.61(7). The estate of the noninsured spouse has no other rights in the policy. *Id.*

A spouse who is neither the policy owner nor the insured may acquire a marital property interest in a policy insuring the life of the other spouse, even though the insured spouse is not the owner. *See* Wis. Stat. § 766.61(3)(d). The amendments to the 1988 Trailer Bill did not address the rights of the noninsured spouse to recover from these policies, but it

is likely that amended section 766.70(6)(b)2. would be interpreted similarly to limit recovery.

### **3. Beneficiary of Deferred-employment-benefit Plan [§ 8.53]**

#### **a. Employee Dies First [§ 8.54]**

Section 766.70(6)(b) allows a surviving spouse to recover his or her former marital property interest in a deferred-employment-benefit plan of the deceased employee spouse if someone other than the surviving spouse is named as beneficiary of more than 50% of the marital property component. Even if a beneficiary designation was made before the spouses' determination date, it may be considered an "arrangement during marriage." *Jackson v. Employee Trust Funds Board*, 230 Wis. 2d 677, 690, 602 N.W.2d 543, 550 (Ct. App. 1999) (holding that designation of third-party beneficiary was "arrangement during marriage" because employee spouse received notice of her right to charge beneficiary while she was married but failed to do so). The Act does not provide for spousal consent to another beneficiary. *See supra* ch. 2. If the Employment Retirement Income Security Act (ERISA) applies to a plan, federal preemption may exist. *See supra* ch. 2. A plan administrator who pays a beneficiary other than the spouse, with or without knowledge of an adverse claim, is protected, *cf.* Wis. Stat. § 766.61(2) (life insurance). Wis. Stat. § 766.62(4); *see supra* ch. 2; *see also* Wis. Stat. § 766.70(7); *infra* §§ 8.59, 12.69 (concerning purchase of deceased employee spouse's interest in deferred-employment-benefit plan from estate). The action by a spouse against the beneficiary must be commenced within the same time limits set forth in section 8.45, *supra*, that is, not later than one year after the employee spouse's death. *Jackson*, 230 Wis. 2d at 690.

#### **b. Nonemployee Dies First [§ 8.55]**

The nonemployee spouse who dies before the employee spouse has no rights in the deferred-employment-benefit plan of the employee. Such rights terminate at the death of the nonemployee. Wis. Stat. §§ 766.62(5), .31(3); *Boggs v. Boggs*, 520 U.S. 833 (1997) (holding that

ERISA preempted nonemployee decedent spouse's children's claims based on Louisiana's community property laws); *see supra* § 2.216.

## C. Third-party Joint Tenant [§ 8.56]

### 1. At Creation of Joint Tenancy [§ 8.57]

The creation of a joint tenancy with a third party by a spouse acting alone using marital property has unique two-stage treatment under the Act. When the gift is made, the nondonor spouse has a right of reimbursement from the donor spouse, the gift recipient, or both for one-half the value of the marital property transferred to third parties in joint tenancy. Wis. Stat. § 766.70(6)(c)1.; *see also supra* §§ 2.241 (classification of property held by spouse in joint tenancy with third person), 8.47–.49 (relating to multiple-party bank accounts). The value of the recovery is one-half the amount determined by dividing the number of joint tenants other than the donor spouse by the total number of joint tenants including the donor spouse. The application of this fraction to the total value of the property subjects the full value of the shares transferred to third parties to this right of reimbursement.

➤ **Example.** A husband holds a marital property asset valued at \$30,000. He creates a joint tenancy between himself and two of his children. His wife has a right of reimbursement for two-thirds of the value, or \$20,000, the sum of the third parties' interests.

The statute does not state whether the recovery is classified as marital property or as the individual property of the nondonor spouse. However, the recovery under section 766.70(6)(c)1. is similar to the recovery under section 766.70(6)(a) for a gift in excess of the value limits of section 766.53 and should be classified in the same manner (i.e., as marital property. *But see* Wis. Stat. § 766.31(7)(e)). Under section 766.70(6)(a), the recovery is marital property if it takes place during the marriage. The recovery is limited to 50% of the value of the transferred property (\$10,000 in the above example) if the recovery occurs after the marriage terminates. If, on the other hand, the recovery during marriage becomes the individual property of the recovering spouse, the amount should also be one-half the value of the transferred interest in marital property. *See supra* § 8.38. A right to reimbursement, rather than a right to property, leaves the operation of the joint tenancy intact. *See* Wis. Stat. Ann.

§ 766.70 Legis. Council Notes—1985 Act 37, §§ 89, 130 to 138 (West 2009). An amount recovered after the marriage terminates is the solely owned property of the recipient.

Although the creation of a joint tenancy with a third person by a spouse using marital property may represent a completed gift to the third person, the value of the marital property interest transferred does not have minimum allowable levels as do gifts to third parties under section 766.53. The entire value, not the amount in excess of \$1,000 or other reasonable amount, may be recovered. Also, only a compensatory judgment is available; the property itself cannot be recovered, as would be possible under section 766.70(6)(a) from a third-party recipient of an outright gift who became a sole owner or a tenant in common. Because the property cannot be recovered, the income on the property from the date of the gift until the date of recovery, whether distributed or retained in the entity held in joint tenancy, also cannot be recovered. The recovering spouse can recover only one-half the value of the marital property transferred in joint tenancy to the third party (one-half of \$20,000 in the above example) because the donor continues to have a severable interest in the property, which has been retained. Wis. Stat. Ann. § 766.70 Legis. Council Notes—1985 Act 37, §§ 89, 130 to 138 (West 2009). Likewise, the nondonor spouse also continues to have a marital property interest in the fractional share of property retained by the donor (i.e., the husband's \$10,000 share in the above example).

If the third-party joint tenant furnishes a portion of the consideration used to acquire the asset held in joint tenancy with a spouse, the creation of the joint tenancy might not be a gift. In that situation, the other spouse's right to recover would arise only if and when the joint tenant spouse predeceased the third-party joint tenant. Section 766.70(6)(c)2. provides for recovery by the nontenant spouse's estate when the nontenant spouse dies first, but it appears to apply only if the creation of the joint tenancy resulted in a gift. If the creation of the joint tenancy did not result in a gift to the third-party joint tenant, then the creation might be considered "an arrangement during marriage involving marital property by a spouse acting alone [that] is intended to be and becomes a gift to a 3rd person upon the death of the spouse." See Wis. Stat. § 766.70(6)(b). Then if the nontenant spouse dies before the tenant spouse, the nontenant spouse's estate could recover from the third person as if the tenant spouse had predeceased the nontenant (thus completing the gift), but with the recovery valued as of the date of death of the nontenant spouse. Wis. Stat. § 766.70(6)(b)2.; *see supra* § 8.49.

Any action under section 766.70(6)(c)1. must be commenced within the earliest of one year after the nondonor has notice of the gift, one year after a dissolution, or one year after the death of either spouse. Wis. Stat. § 766.70(6)(c)1.

## 2. At Death of Tenant Spouse [§ 8.58]

If the asset continues to be held in joint tenancy until the death of the tenant spouse, the nontenant spouse has a second opportunity to recover reimbursement (e.g., the \$10,000 interest retained by the donor spouse in the example at section 8.57, *supra*). Wis. Stat. § 766.70(6)(c)2. Recovery may be from the decedent's estate, the surviving joint tenant, or both. *Id.* Recovery is measured by a fraction of the date of death value of the entire asset equal to one-half the quotient resulting from dividing one by the total number of joint tenants immediately before the death of the tenant spouse. Wis. Stat. § 766.70(6)(c)2. Although there is no statutory provision classifying the amount recovered, the amount would of necessity be the solely owned property of the surviving spouse. The purpose of this second recovery is to reimburse a spouse for any appreciation in the retained property that occurred between the date of the gift and the tenant spouse's date of death. *See* Wis. Stat. Ann. § 766.70 Legis. Council Notes—1985 Act 37, §§ 89, 130 to 138 (West 2009).

A recovery after the death of the tenant spouse under section 766.70(6)(c)2. is not reduced by a prior recovery of amounts received during the marriage for the joint tenancy property under subparagraph 1. because the two recoveries are for different property interests. The first recovery under subparagraph 1. is for the portion transferred by the donor spouse. The second recovery under section 766.70(6)(c)2. is for the portion of the property that was marital property retained by the donor until death.

There is no provision for the intervening death of a third-party joint tenant if more than one third party had been given an interest as a joint tenant in marital property.

➤ **Example.** Assume that a husband holds a marital property asset valued at \$30,000 and creates a joint tenancy with X and Y. The wife may recover \$10,000 each from X and Y as marital property, thereby reimbursing the marital estate for the \$20,000 transferred. The wife



continues to have a one-half marital property interest in the \$10,000 portion that the husband retained. Then X dies, leaving the husband and Y as joint owners. When the husband dies, assume that the property has increased in value to \$100,000. The wife may again recover from Y, who now owns the entire property. The wife's recovery from Y is one-half of one-half the value of the property, \$25,000. If X had not died before the husband, the wife would have recovered one-half of one-third (one-third being the fractional share owned by the husband at death), \$16,666. The intervening death of X allows the wife to recover from property covered by the first recovery under section 766.70(6)(c)1., which was returned to the husband because of X's death.

An action under section 766.70(6)(c)2. must be commenced by the surviving spouse not later than one year after the death of the "decedent" spouse, apparently referring to the death of the tenant spouse. The property is valued as of the date of the tenant spouse's death, which gives the survivor no right to income or appreciation in value after the tenant spouse's death.

If the nontenant spouse predeceases the tenant spouse, the action must be commenced not later than one year after the "decedent's" death. The statute is not clear whether the term decedent's death refers to the death of the tenant or the nontenant. However, it appears that the one-year period begins to run when the nontenant dies. The portion of the property subject to reimbursement is measured "as if the tenant spouse had predeceased the spouse with the right of reimbursement, but is valued at the date of death of the spouse with the right of reimbursement." Wis. Stat. § 766.70(6)(c)2. Therefore, the nontenant spouse's estate or other successor in interest must commence an action against the tenant spouse (or his or her estate, if the tenant spouse dies within the year after the death of the nontenant spouse), or the other joint tenants, or both, not later than one year after the nontenant spouse's death.

#### **D. Estate Holding Life Insurance Policy or Deferred-employment-benefit Plan [§ 8.59]**

The surviving spouse has the right to purchase from the decedent's estate the decedent's interest in any life insurance policy or deferred-employment-benefit plan described in sections 766.61 and .62,

respectively, if all or part of the policy or plan is included in the deceased spouse's estate. Wis. Stat. § 766.70(7). Sections 766.61 and .62 refer to policies insuring a spouse's life or deferred-employment-benefit plans attributable to a spouse's employment. The remedy under section 766.70(7) is necessarily limited to a policy owned by the decedent on the surviving spouse's life or a plan attributable to the decedent's employment. Wis. Stat. §§ 766.61, .62. This right to purchase may be important when the decedent spouse owned a policy on the survivor's life and the survivor wishes to retain the policy because he or she either is no longer insurable or is unable to obtain favorable rates.

In the case of life insurance, the interest of the decedent in a policy must be in one insuring the life of the surviving spouse, since any right the surviving spouse has to recover a marital property interest in a policy insuring the life of the decedent would be transferred to the proceeds in the hands of a third-party beneficiary. *See* Wis. Stat. § 766.70(6)(b). In the case of a deferred-employment-benefit plan, the decedent's interest in a plan attributable to the employment of the survivor terminates at the death of the nonemployee, and the decedent nonemployee's estate or heirs have no rights in the plan. Wis. Stat. § 766.62(5).

The 1988 Trailer Bill clarified the requirement that the estate of a noninsured spouse that has a marital property interest in a life insurance policy owned by and insuring the life of the surviving spouse must sell that interest to the surviving spouse upon the exercise of the surviving spouse's right to purchase under section 766.70(7). Section 766.61(7) clarifies the effect of the surviving spouse's failure to purchase the marital property interest of a decedent spouse. Failure to do so limits the recovery by the noninsured spouse's estate to one-half the noninsured spouse's marital property interest in the interpolated terminal reserve of a nonterm policy and in the unused portion of the premium of a term policy on the date of the noninsured spouse's death. Wis. Stat. § 766.61(7); *see also supra* § 8.52.

Under section 766.61(3)(d), a spouse acquires an interest in a policy that insures a spouse's life but that is owned by another person or entity if premiums are paid with marital property. It appears that the surviving spouse may also purchase the decedent's interest in this type of policy.

The cost to the surviving spouse is the fair market value of the policy or plan. The purchase must be made within 90 days after the earlier of

either receiving a copy of the inventory listing the policy or plan or discovering the existence of the policy or plan. Wis. Stat. § 766.70(7).

## **V. Procedure [§ 8.60]**

### **A. In General [§ 8.61]**

The Act does not specify the procedures governing actions under section 766.70. Therefore, the general rules of civil procedure apply, *see* Wis. Stat. chs. 801–807, including the right to trial by jury. Wis. Stat. § 801.01(2).

Actions affecting the family have special procedural rules outlined in chapter 767. Unlike a divorce, an interspousal action under section 766.70 is commenced with a summons and complaint, not a petition, and the parties are plaintiff and defendant, not petitioner and respondent. An action for an interspousal remedy cannot be combined initially with an action for divorce because actions affecting the family, set forth in section 767.001(1), do not include interspousal remedies. *See also* Wis. Stat. § 805.05 (describing requirements for consolidation of actions and for separate trials). Also, the contents of the petition are specified by statute in an action affecting the family, *see* Wis. Stat. § 767.215(2), and there are no provisions for allegations appropriate for an interspousal remedy. Nevertheless, in some cases, if not most, the same issues and the same fact situations may be involved in the dissolution action and in the action for an interspousal remedy. It appears to be appropriate to assign both cases to the same judge, even if the actions are not consolidated.

Once an action for dissolution is filed, no action under section 766.70 may be commenced, and any such action that is pending may be consolidated with the dissolution action. Wis. Stat. § 767.331; *see also* Wis. Stat. § 805.05. The constitutionality of section 767.05(7) (now section 767.331) was considered in *Haack v. Haack*, 149 Wis. 2d 243, 440 N.W.2d 794 (Ct. App. 1989). The wife argued that this provision was unconstitutional on the grounds that the bar to a section 766.70 claim violated her right to jury trial, was gender biased, and denied her equal protection of the law. The court noted that because of her pending divorce, the wife had no statutory cause of action under section 766.70; therefore, she had no right to a jury trial. Furthermore, even though the Act was an outgrowth of the women's rights movement, it was gender

neutral because it created rights for both spouses. Finally, the court found that there was no denial of equal protection because there is a rational basis for treating an ongoing marriage and a dissolving marriage differently. Property rights can be of primary concern in an ongoing marriage; hence the protections of section 766.70 were provided by the Act. In a dissolving marriage, however, other interests arise, such as equitable distribution of property and support of children. Since a state may place reasonable limits on the rights of parties, the court of appeals concluded that section 767.05(7) (now section 767.331) is constitutional. 149 Wis. 2d at 250–56; *see also Gardner v. Gardner*, 175 Wis. 2d 420, 432–33, 499 N.W.2d 266 (Ct. App. 1993) (applying holding from *Haack*).

The pendency of a dissolution action is not necessarily an impediment to an action between spouses that is unrelated to an interspousal remedy. In *Knafelc v. Dain Bosworth, Inc.*, 224 Wis. 2d 346, 591 N.W.2d 611 (Ct. App. 1999), the wife brought an action against her husband and his brokerage firm alleging securities fraud, vicarious liability, and negligent supervision in connection with the management of a securities account in her name that was funded with the couple's marital property. Even though the dissolution action had been filed earlier, the court held that the action was based on a relationship independent of the marriage and could be maintained.

To the extent that procedural and substantive rights under chapters 766 and 767 conflict in an action for an interspousal remedy, chapter 767 controls. Wis. Stat. § 767.331. Except for the fact that there is no right to a jury trial at divorce, there do not appear to be conflicts since the rights conferred in the two chapters are not mutually exclusive. The facts of particular cases may warrant the commencement of both actions. See section 11.4, *infra*, for examples of such instances.

The circumstances under which an interspousal remedy is appropriate during the pendency of a dissolution, provided the interspousal action is commenced before the dissolution, are different from the circumstances under which a temporary order under section 767.225 is appropriate. An interspousal remedy involves the classification and control of property, *see* Wis. Stat. § 766.70, whereas the relief that may be requested in a proceeding before the court is primarily related to temporary custody and support, *see* Wis. Stat. § 767.225. The court is not authorized to grant relief enumerated under section 766.70 pending the divorce. Section 766.70 has no provision for temporary relief, other than the temporary

limitation of management and control on the grounds specified in section 766.70(4); such temporary limitation under section 766.70(4) is relief ordered by the final decree, not relief pending the final decree. However, a temporary injunction under section 813.02 may sometimes be appropriate.

## **B. Incompetent Spouse [§ 8.62]**

If a spouse subject to guardianship has a claim against the other spouse, the effect of the various statutes of limitation is not clear. The general rule is that a statute of limitation is tolled for the period of a plaintiff's disability, and that the action may be commenced within two years after the disability ceases. Wis. Stat. § 893.16(1). However, if the disability is a result of mental illness, the time limit cannot be extended by more than five years. *Id.*

The appointment of a guardian usually has no effect on a statute of limitation that has been suspended. 51 Am. Jur. 2d *Limitation of Actions* § 233 (West, WESTLAW current through March 2010). An exception applies if the statute conferring authority on the guardian directs that all necessary actions regarding the ward's estate be brought by the guardian. *Id.* Section 54.19 enumerates the duties of the guardian of the estate, cautioning that he or she must act "to provide a ward with the greatest amount of independence and self-determination with respect to property management in light of the ward's functional level, understanding, and appreciation of his or her functional limitations and the ward's personal wishes and preferences with regard to managing the activities of daily living." Even though a guardian may not be required to bring an action, he or she should not be prohibited from doing so. *See Young v. State*, 401 N.Y.S.2d 955 (Ct. Cl. 1978). The provision limiting the extension of the limitation to five years, section 893.16(1), may impose a duty on the guardian to commence an action against the ward's spouse if it appears that more than five years will pass before the disability ceases or before the ward's death results in the cause of action passing to the ward's personal representative, *see* Wis. Stat. § 893.22 (limitation in case of death).

## **VI. Sample Forms [§ 8.63]**

➤ **Note.** Additional forms for interspousal remedies appear in Leonard L. Loeb et al., *System Book for Family Law* (State Bar of Wisconsin CLE Books 6th ed. 2007 & Supp.).

### **A. Sample Complaint for Breach of Good-faith Duty [§ 8.64]**

#### **1. Introduction [§ 8.65]**

The following is a sample complaint for breach of the good-faith duty under the Act. It is a sample only and does not purport to be all-inclusive. Each pleading must be tailored to the parties' circumstances.

4. The parties have not entered into any marital property agreement or any other marriage agreement affecting the economic incidents of their marriage.

5. On November 13, 2009, defendant co-signed a note to First National Bank in the amount of \$100,000 for the purpose of inducing the bank to make a loan to XYZ Enterprises, Inc., a corporation solely owned and operated by Jeff Smith, defendant's brother. Defendant also signed a separate statement that the loan was being incurred for a family purpose. Defendant received no consideration for executing the note. Plaintiff did not consent to defendant's co-signing the note and strenuously objected when informed of his plan to execute the note.

6. The note of XYZ Enterprises, Inc. is not in default.

7. Plaintiff is the sole proprietor of a business known as Jane's Café. The business was commenced in July 1996 and is marital property. Plaintiff's one location has been successful, and she wishes to expand to two additional locations.

8. Plaintiff requires a loan of \$30,000 for the cost of opening such additional locations and for initial operations. Because of the nature of the assets of the business, the loan would be largely unsecured. Before execution of the note of XYZ Enterprises, Inc., defendant knew that plaintiff planned to expand the business and that she would need credit to do so.

9. Plaintiff has been denied credit for such purpose at three lending institutions, causing damage to plaintiff's business. Plaintiff is informed and believes that such credit would not have been denied absent defendant's co-signing the note of XYZ Enterprises, Inc.

WHEREFORE, plaintiff requests that the court:

1. Find that defendant's execution of the \$100,000 note to First National Bank in consideration for a loan granted to XYZ Enterprises, Inc., constitutes a violation of the good-faith duty between spouses;

2. Award plaintiff \$30,000 compensatory damages or the expected amount of lost profits caused by defendant's impairment of her creditworthiness, or require defendant to take such action as is necessary to qualify plaintiff for a loan of \$30,000;

3. Classify any such recovery in accordance with its findings;

4. Enjoin defendant from incurring any further extensions of credit that may subject the parties' marital property to satisfaction of said obligations;



5. Order the defendant to provide anyone from whom he requests an extension of credit with a copy of the judgment in this action; and

6. Grant such other relief as it determines to be equitable under the circumstances.

***[Add jury demand if desired]***

JURY DEMAND

Plaintiff demands a trial by a jury of *(six)* *(twelve)*.

Dated: \_\_\_\_\_

---

Attorney for Plaintiff  
Jones Law Offices  
808 Oak Street  
Milwaukee, WI 53299  
State Bar # 000007

## **B. Sample Complaint to Add a Name to Marital Property [§ 8.67]**

### **1. Introduction [§ 8.68]**

The following is a sample complaint to add a name to marital property. It is a sample only and does not purport to be all inclusive. Each pleading must be tailored to the parties' circumstances.

John Smith, by his attorneys, as a complaint against the defendant, states as follows:

1. John Smith, plaintiff, is an adult and resides at 123 Main St., Milwaukee, Wisconsin.
2. Jane Smith, defendant, is an adult and resides at 123 Main St., Milwaukee, Wisconsin.
3. Plaintiff and defendant were married to each other in Milwaukee, Wisconsin, on September 25, 1990, and have been continuously married since that date. No action for divorce or legal separation has been commenced or is now pending in any court.
4. The parties have not entered into any marital property agreement or any other marriage agreement affecting the economic incidents of their marriage.

5. Defendant is the holder of a certificate of deposit with ABC Bank, #862-519, in the principal amount of approximately \$50,000. Upon information and belief, all or part of the account is marital property.

6. Real estate located at 456 Maple Lane, Milwaukee, Wisconsin, is held in the defendant's name and is more fully described as:

Lot 1, Block 2, Jones Subdivision, City of Milwaukee, County of Milwaukee, State of Wisconsin.

Upon information and belief, all or part of the real estate is marital property.

7. No party other than plaintiff and defendant has an interest in either asset.

8. Neither asset is the type of property described in Wis. Stat. § 766.70(3)(a)–(d).

9. Plaintiff is a co-owner of the property and wishes to participate equally in the management and control of the property.

WHEREFORE, plaintiff requests that the court enter an order adding his name in the conjunctive form to the record ownership of the above marital property.

***[Add jury demand if desired]***

JURY DEMAND

Plaintiff demands a trial by a jury of *(six) (twelve)*.

Dated: \_\_\_\_\_

---

Attorney for Plaintiff  
Jones Law Offices  
808 Oak Street  
Milwaukee, WI 53299  
State Bar # 000007

**C. Sample Complaint to Limit Management and Control, to Divide Current and Future Obligations, and to Classify Future Acquisitions of Property**  
**[§ 8.70]**

**1. Introduction [§ 8.71]**

The following is a sample complaint to limit management and control, to divide current and future obligations, and to classify future acquisitions of property. It is a sample only and does not purport to be all-inclusive. Each pleading must be tailored to the parties' circumstances.

Jane Smith, by her attorneys, as a complaint against the defendant, states as follows:

1. Jane Smith, plaintiff, is an adult and resides at 123 Main St., Milwaukee, Wisconsin. She is employed by the Milwaukee Candy Company.
2. John Smith, defendant, is an adult, and his residence is unknown. He is employed by Johnson and Associates.
3. Plaintiff and defendant were married to each other in Milwaukee, Wisconsin, on September 25, 1990, and have been continuously married since that date. No action for divorce or legal separation has been commenced or is now pending in any court. The parties have two minor children: George, born December 24, 1999, and Martha, born January 12, 2002.

4. The parties have not entered into any marital property agreement or any other marriage agreement affecting the economic incidents of their marriage.

5. A money market account with ABC Bank, #862-519, in the principal amount of approximately \$50,000, is held in the defendant's name. Upon information and belief, all or part of the account is marital property.

6. Real estate located at 456 Maple Lane, Milwaukee, Wisconsin, which is held in the defendant's name, is more fully described as:

Lot 1, Block 2, Jones Subdivision, City of Milwaukee, County of Milwaukee, State of Wisconsin.

Upon information and belief, all or part of the real estate is marital property.

7. No party other than plaintiff and defendant has an interest in either asset.

8. Neither asset is the type of property described in Wis. Stat. § 766.70(3)(a)–(d).

9. Since December 2009, defendant has failed to collect rent for, make repairs to, and purchase insurance for the property at 456 Maple Lane. The final mortgage payment of \$25,000 on the real estate is due April 1, 2010. It will be necessary to use funds from the money market account to pay the mortgage and avoid a default.

10. Plaintiff has received numerous telephone calls from creditors relating to obligations incurred by defendant since he moved out of the family home in December 2009.

11. Defendant has made large withdrawals from the parties' money market account held in his name and has incurred an unreasonable amount of indebtedness. Plaintiff fears that he will continue to do so in the future.

12. The foregoing acts and omissions constitute gross mismanagement of the parties' marital property.

13. Plaintiff wishes to have management and control of the above mentioned marital property assets transferred to her so that such assets may be conserved.

14. Plaintiff fears that her wages may be garnished by creditors of the defendant, and she wishes to protect those wages to better enable her to support herself and the parties' minor children.

WHEREFORE, plaintiff requests that the court:

1. Order that plaintiff have management and control of marital property held by defendant;

2. Divide the existing obligations of the parties;

3. Declare that future obligations are the responsibility of the incurring spouse;

4. Declare that property acquired in the future by either party is the individual property of the acquiring spouse;

5. Require both parties to disclose the order of the court in this case to any future creditor before an obligation is incurred; and

6. Grant the plaintiff such other relief as is appropriate under the circumstances.

***[Add jury demand if desired]***

JURY DEMAND

Plaintiff demands a trial by a jury of *(six) (twelve)*.

Dated \_\_\_\_\_

---

Attorney for Plaintiff  
Jones Law Offices  
808 Oak Street  
Milwaukee, WI 53299  
State Bar # 000007



## Income and Transfer Taxes

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## **I. Scope of Chapter [§ 9.1]**

This chapter is not intended to be a comprehensive treatise on the ways that federal and Wisconsin income, estate and gift taxes affect married couples generally nor is it intended to be a complete guide to all of the tax issues involved with divorce. Rather, this chapter focuses for the most part on some of the specific tax issues resulting from the Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or the Wisconsin Marital Property Act] and Wisconsin's adoption of a system of community property.<sup>1</sup>

Wisconsin's status as a community property state for federal tax purposes was confirmed in 1987, when the IRS issued Revenue Ruling

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<sup>1</sup> All references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189; all references to the United States Code (U.S.C.) and Internal Revenue Code (I.R.C.) are current through Public Law Number 111-166 (excluding Pub. L. Nos. 111-148, -152, and -159) (May 19, 2010); and all references to the Code of Federal Regulations (C.F.R.) and Treasury regulations (Treas. Reg.) are current through 75 Fed. Reg. 27,140 (May 13, 2010). Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

87-13, 1987-1 C.B. 20 (1987). In this ruling, the IRS formally recognized that the property rights of spouses under the Marital Property Act are community property rights and should be treated as such for purposes of applying federal tax laws.

## **II. Income Tax Considerations [§ 9.2]**

### **A. Federal Income Tax: Joint Return Filing and the “Innocent-spouse” Rules [§ 9.3]**

Many married taxpayers choose to file joint income tax returns because of certain benefits this filing status allows. A husband and wife may generally file a joint return in which they aggregate income and deductions, even if one of the spouses has neither gross income nor deductions. The tax on the joint return is determined under a rate schedule that computes the tax at the usual rate on one-half of the aggregate taxable income and doubles that amount. This, in effect, gives the spouses the same tax treatment that they would have under a community property system if all the income were community and each spouse owned half. It also partially blunts the progressivity of the income tax rates. *Compare* I.R.C. § 1(a) with § 1(d). A joint return may not be filed, however, if either spouse was at any time during the taxable year a nonresident alien (unless a special election is filed under I.R.C. § 6013(g)) or if one spouse dies and the surviving spouse remarries before the close of the taxable year. I.R.C. § 6013(a).

A potential downside to filing a joint return is that both spouses are jointly and severally liable for any taxes and interest or penalties due, even if they later divorce. I.R.C. § 6013(d)(3). This is true even if the divorce decree states that one spouse will be responsible for any amounts due with respect to previously filed joint returns. *Pesch v. Commissioner*, 78 T.C. 100 (1982). Moreover, a spouse may be held responsible for the entire amount due, even if the other spouse earned all of the income or claimed improper deductions or credits.

Joint and several liability can lead to significant hardship for individuals who are divorced or widowed when, unbeknownst to them, there are tax deficiencies as a result of undisclosed income or unwarranted overstatements of a deduction, credit, or basis by a former spouse from whom collection is impossible because of death,

disappearance, or insolvency. Although such situations cry out for equitable relief for spouses who were unaware of the transactions that resulted in the deficiency, the federal tax laws for many years were not especially sympathetic to “innocent spouses.” See I.R.C. § 6013(e) (repealed by the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat. 685). In July 1998, however, relief for such aggrieved spouses came in the form of I.R.C. § 6015, which provides three potential avenues of relief:

1. **Innocent-spouse relief.** The traditional (though now more lenient) form of innocent-spouse relief remains available if (a) a joint return was filed, (b) there is an understatement attributable to erroneous items of one spouse, (c) the other spouse did not know or have reason to know of the understatement, and (d) taking into account all facts and circumstances, it would be inequitable to hold the other spouse liable. Partial relief is available if the innocent spouse knew of some, but not all, of the understatements attributable to the other spouse. See I.R.C. § 6015(b).

In issuing final regulations for I.R.C. § 6015, the IRS clarified that the standards for *knowledge or reason to know* that were developed under former I.R.C. § 6013(e) should continue to be used in determining whether a spouse requesting relief had knowledge or a reason to know that would result in the denial of a request for innocent-spouse relief. Relief from Joint and Several Liability, 67 Fed. Reg. 47,278, 47,288 (July 18, 2002). Under the regulations, a requesting spouse knows or has reason to know of an understatement if he or she actually knew of the understatement or if a reasonable person in similar circumstances would have known of the understatement. All of the facts and circumstances are considered when determining whether the requesting spouse had reason to know, including the following: the nature and amount of the erroneous item relative to the other items; the couple’s financial situation; the requesting spouse’s educational background and business experience; the extent of the requesting spouse’s participation in the activity that resulted in the erroneous item; whether the spouse failed to inquire about reported or omitted items that a reasonable person would question; and whether the item represented a departure from a recurring pattern reflected in returns filed in prior years. See Treas. Reg. § 1.6015-2(c).

2. **Separate-liability election.** Spouses who are divorced, legally separated, or living apart may make a separate-liability election with

respect to a joint return filed by them that gives rise to a deficiency. Such an election limits a spouse's allocable portion of a deficiency to the amount attributable to the income and deductions of that spouse. With certain exceptions, the election accomplishes this result by allocating income and deductions to the spouse responsible for earning the income or creating the deduction. The burden of proof with respect to establishing the portion allocable is on the electing spouse. The election does not apply with respect to a deficiency, however, if (a) the spouse received a tax benefit from an item otherwise allocable to the other spouse, (b) the electing spouse had actual knowledge of any item resulting in a deficiency, or (c) assets are transferred between the spouses with a tax avoidance motive. *See* I.R.C. § 6015(c).

The standard of actual knowledge set forth in I.R.C. § 6015(c) is much narrower than the “know or had reason to know” test used in determining eligibility for innocent-spouse relief. Moreover, the IRS has the burden of demonstrating actual knowledge by a preponderance of the evidence. Treas. Reg. § 1.6015-3(c)(2)(i). For purposes of determining when the requesting spouse has actual knowledge, the regulations set forth tests to be used in specific circumstances, such as the omission of income or an erroneous deduction or credit. One factor that can be relied on by the IRS in establishing actual knowledge, however, is whether the requesting spouse made a deliberate effort to avoid learning about the erroneous item so as to be shielded from liability. Joint ownership of the property that resulted in the erroneous reporting of an item is another factor supporting a finding of actual knowledge, but joint ownership by mere application of community property laws is not sufficient. Rather, a requesting spouse who resided in a community property state at the time the return was signed will be considered to have had an ownership interest in an item only if the requesting spouse's name appeared on the ownership documents or if there is otherwise an indication that the requesting spouse asserted dominion and control over the item. Treas. Reg. § 1.6015-3(c)(2)(iv). *But see Rowe v. Commissioner*, T.C.M. (CCH) 1020 (2001) (husband established and then withdrew funds from an individual retirement account (IRA) opened in wife's name without her knowledge; court allocated taxable distribution to husband reasoning that wife's only connection to the account was use of her name).

➤ **Example.** H and W are Wisconsin residents. H opens a bank account, in his name only, in which he deposits a portion of his paychecks. H fails to report interest earned on the account on the



couple's joint tax return. Under section 766.34, W owns one-half of the bank account. Because W is not named as an owner on the account, however, she will not be considered as having an ownership interest in the account for purposes of applying Treasury Regulation § 1.6015-3(c)(2)(iv), unless there is some other indication that she asserted dominion and control over the account.

The Tax Court has also articulated standards for what constitutes *actual knowledge* for purposes of I.R.C. § 6015(c). In *Cheshire v. Commissioner*, 115 T.C. 183 (2000), *aff'd*, 282 F.3d 326 (5th Cir. 2002), the Tax Court held that actual knowledge means an “actual and clear awareness” of the item and does not require specific knowledge of the tax consequences arising from the item. In this case, the husband received a distribution from his retirement account but failed to include a portion of it on the couple's joint return. When questioned by his wife about the tax consequences of the distribution, he falsely told her that it was not taxable. The Tax Court, however, found that this misinformation was not relevant to the actual knowledge inquiry. Instead, the court found that since the wife had actual knowledge that the omitted income existed and she knew the amount of the income, she was not entitled to relief under I.R.C. § 6015(c). *See also Wiksell v. Commissioner*, 90 F.3d 1459 (9th Cir. 2000) (holding that actual-knowledge inquiry focuses on whether taxpayer had knowledge of any item giving rise to deficiency, not on tax deficiency itself); Treas. Reg. § 1.6015-3(c)(2)(i)(A). But see *Menendez v. Commissioner*, 94 T.C.M. (CCH) 707 (2007), in which the Tax Court rejected the ex-husband's argument that the taxpayer wife must have known of an IRA distribution because of a reference in the marital inventory list to the IRA's zero balance. The court said the list was based on information existing as of the list-signing date, which postdated the tax year at issue and did not specify when the withdrawal was made; there was no other evidence that the wife had any actual knowledge of the withdrawal in the subject year.

3. Equitable relief. If the spouse is not eligible to make the innocent-spouse or separate-liability election, relief may still be available if, taking into account all facts and circumstances, it would be inequitable to hold the spouse responsible for the joint tax return deficiency. *See* I.R.C. § 6015(f). The IRS has issued Rev. Proc. 2003-61, 2003-32 I.R.B. 296 (superseding Rev. Proc. 2000-15, 2000-1 C.B. 447), which provides guidance on the circumstances under which equitable relief will be granted under I.R.C. § 6015(f). *See*

*also Innocent Spouse Relief*, IRS Publ'n 971, *available at* <http://www.irs.gov/pub/irs-pdf/p971.pdf> (revised Apr. 2008).

In determining whether relief is available under I.R.C. § 6015, items of income, credits, and deductions are generally allocated to the spouses without regard to community property laws. Instead, an erroneous item is attributed to the individual whose activity gave rise to such item. I.R.C. § 6015(a); *see also* Treas. Reg. § 1.6015-1(a)(1). For example, if a Wisconsin married couple is assessed with an income tax deficiency as a result of the husband understating his wages on a jointly filed return, the deficiency will be allocated to the husband even though such income would be considered marital property. Similarly, if an income tax deficiency is assessed as a result of both spouses underreporting their income, the deficiency will be allocated to the spouses pro rata, in accordance with their respective underreported amounts.

➤ **Example.** On April 15, 2010, H and W, a Wisconsin married couple, file a joint income tax return for the 2009 taxable year. In August 2011, the IRS proposes a deficiency with respect to the 2009 joint return. A portion of the deficiency is attributable to \$50,000 of H's unreported income from his dental practice. The remainder of the deficiency is attributable to \$30,000 of unreported income from W's consulting business. This income is considered marital property under section 766.31(4).

In November 2011, H and W file for divorce and W timely elects to allocate the deficiency under I.R.C. § 6015(c). Although under Wisconsin's marital property laws one-half of H's income from his dental practice is W's and one-half of W's consulting income is H's, for purposes of determining relief under I.R.C. § 6015 the marital property classification of such income is ignored and the \$50,000 of H's unreported income from his dental practice is allocated to him and the \$30,000 of unreported income from W's consulting business is allocated to her.

Community property laws are not disregarded, however, with respect to the attribution of gross income derived from property. For example, rental income (when neither spouse renders substantial services in managing the rental property) will be deemed to be the income of both spouses in equal shares.

An election or request for relief under I.R.C. § 6015 is made by filing Form 8857 (Request for Innocent Spouse Relief (and Separation of Liability and Equitable Relief)) no later than two years after collection activity is initiated by the IRS. A spouse requesting relief may elect to be considered under all three categories for relief provided by I.R.C. § 6015. A statement signed under penalties of perjury must be attached to the form, explaining the grounds for relief under each category requested. Only one Form 8857 needs to be filed even if relief is sought for more than one tax year. A personal representative can make the election for innocent-spouse relief or allocation of liability on behalf of a deceased taxpayer. Rev. Rul. 2003-36, 2003-18 I.R.B. 849. The Tax Court, however, has held that the death of a spouse does not satisfy the “not married” condition for purposes of making the separate-liability election and that a personal representative can elect innocent-spouse or separate-liability relief only if the deceased spouse satisfied the eligibility requirements before death. *Jonson v. Commissioner*, 118 T.C. 106 (2002), *abrogated on other grounds by Porter v. Commissioner*, 132 T.C. 203 (2009).

➤ **Practice Tip.** As a safeguard in the event that the client fails to qualify for innocent-spouse relief or is found ineligible to elect a separate allocation of liability, a detailed statement should be attached to Form 8857 also, as support for a claim for equitable relief.

Upon receipt of a spouse’s Form 8857 requesting relief, the IRS must send a notice of the election to the nonrequesting spouse and give him or her an opportunity to submit information relevant to its determination. See Rev. Proc. 2003-19, 2003-5 I.R.B. 371 (providing guidance on the administrative appeal rights of both the requesting spouse and nonrequesting spouse). The IRS will generally share any information submitted by one spouse that is requested by the other spouse unless “it would impair tax administration.” Treas. Reg. § 1.6015-6(a)(1).

➤ **Practice Tip.** These notification provisions could prove disconcerting for aggrieved spouses who fear that filing a claim for relief will result in possible retaliation from a former spouse and who do not want their whereabouts revealed. The IRS *Internal Revenue Manual* provides that the IRS will omit from shared documents any information that could reasonably identify a spouse’s location. The IRS further recommends that spouses concerned about retaliation write the term “Potential Domestic Abuse Case” on the top of their

Form 8857 and attach a supporting statement with relevant details. These steps will alert IRS personnel to the sensitivity of the requesting spouse's situation and the information provided.

Historically, it has been unclear whether an innocent spouse is entitled to a refund under I.R.C. § 6015(g) for community property assets used to pay the other spouse's federal tax liabilities. In a case of first impression, however, the Tax Court held in *Ordlock v. Comm'r*, 126 T.C. 47 (2006), *aff'd*, 533 F.3d 1136 (9th Cir. 2008), that a taxpayer who had been granted innocent-spouse relief was not entitled to a refund for tax payments made from community property.

The taxpayer and her husband were California residents and filed joint income tax returns. The IRS made a number of assessments for additional taxes, penalties, and interest attributable to underreporting of income by the husband on such returns. The IRS granted innocent spouse relief to the taxpayer under I.R.C. § 6015(b), relieving her from joint and several liability for the outstanding tax due, but applied numerous tax payments made by the couple to the husband's understatements. All but one of these tax payments were from the couple's community property assets, with the other coming from the taxpayer's separate property.

The wife sought a refund from the IRS, asserting that the statutory language under I.R.C. § 6015(g) providing that a refund must be allowed to an innocent spouse "notwithstanding any other law or rule of law" took precedence over California's community property laws. The IRS agreed that the taxpayer was entitled to a refund for the one payment made from her separate property. The IRS, however, asserted that the taxpayer was not entitled to a refund of community property assets because, under I.R.C. § 6321, the IRS's tax lien attached to the entire amount of the couple's community property.

The court denied the refund request, holding that I.R.C. § 6015(g) should not be read to ignore or trump state property laws. The court instructed that under I.R.C. § 6015 only the finding that a spouse is innocent and entitled to relief shall be determined without regard to community property laws, not the right for refunds or the ability of the IRS to attach liens to community property. Ruling otherwise, the court reasoned, would lead to the complex administrative problem of trying to determine whether tax payments were made from community or separate property. Additionally, the court explained that allowing an innocent

spouse a refund for his or her portion of the tax payments would create the potential for abuse in which a couple could recoup their payments by having the innocent spouse make the payments.

In Revenue Ruling 2004-71, 2004-30 I.R.B. 74, the IRS provided guidance regarding the amount of an overpayment from a joint income tax return that the IRS may offset against one spouse's separate tax liability for married taxpayers domiciled in Wisconsin.

The ruling provides that the IRS will use a five-step process to determine the amount of a joint overpayment that it may offset against the separate federal tax liability of one spouse. Specifically, in making this determination, the IRS will do the following:

1. Identify the underlying source of the overpayment;
2. Characterize the underlying source of the overpayment as either separate or marital property;
3. Offset the liable spouse's share of the overpayment from a marital property source against the liable spouse's separate tax liability;
4. Determine whether Wisconsin law permits the IRS to reach the nonliable spouse's share of the overpayment from a marital property source; and
5. Determine whether Wisconsin law permits the IRS to reach a portion of the overpayment from a separate property source of the liable spouse or the nonliable spouse.

The ruling applies this five-step process to three specific fact situations involving Wisconsin married couples.

➤ **Note.** An innocent spouse may have a remedy against his or her spouse under section 766.70(5) if the IRS recovers marital property not available to a creditor under state law because the tax debt is not a family-purpose debt. *See supra* § 8.36. Equitable factors such as whether the spouses are separated may be considered in determining whether the innocent spouse has a right of reimbursement. A remedy under section 766.70(1) for a breach of the duty of good faith may also be available to an innocent spouse for the recovery of taxes paid as a result of the actions of his or her spouse. *See supra* § 8.18.

## **B. Federal Income Tax: Allocation of Community Income If Spouses File Separate Returns [§ 9.4]**

### **1. Spouses Living Apart; Innocent-spouse Provisions [§ 9.5]**

Normally, it is advantageous for spouses to file a joint federal income tax return. It may be impossible to do so, however, if a couple is estranged but not yet divorced and cannot agree on filing a joint return. In a community property state, this can result in serious inequity to a spouse who is not generating significant income. Under state community property laws, each spouse has a present vested interest in community income and property, and the federal gross income of each spouse includes one-half of the community income, so each spouse is liable for income taxes on that share. *United States v. Mitchell*, 403 U.S. 190, 196–97 (1971); *Poe v. Seaborn*, 282 U.S. 101 (1930). Therefore, if one spouse in a community property jurisdiction generates nearly all of the family income but turns over none or only a small share of it to the other spouse, the filing of a separate return may provide a significant advantage to the earning spouse. Specifically, the earning spouse is required to report only one-half of the income and pay tax on that amount. The spouse who is not generating the income, on the other hand, ends up with both a reporting burden (for one-half of the spouses' total community income) and a significant tax liability (the tax on that half of the income). The affected spouse, however, often has none of the income (and generally no other assets) with which to pay the tax liability.

To address this inequity, Congress enacted I.R.C. § 66, which provides three separate means by which a spouse in a community property state can be relieved from income tax liability on his or her community property share of the other spouse's income. The first of these relief provisions is narrow in scope and applies only to spouses who live apart for the entire taxable year and who also meet the following requirements of I.R.C. § 66(a):

1. They must be married to each other at some time during the calendar year.
2. They must not file a joint return with each other for a taxable year beginning or ending in the calendar year.

3. One or both of the spouses must have earned income (as defined in I.R.C. § 911(d)(2)) that is community income as defined under applicable community property laws.
4. No portion of the earned income may be transferred directly or indirectly between the spouses before the close of the calendar year.

To satisfy the “living apart” requirement necessary for relief under I.R.C. § 66(a), the spouses must maintain separate residences. Spouses who maintain separate residences because of a temporary absence, such as military service, will not be considered to be living apart for purposes of I.R.C. § 66(a). Treas. Reg. § 1.66-2(b).

A transfer of a de minimis amount of earned income between spouses will not be considered a violation of the requirements of I.R.C. § 66(a). Treas. Reg. § 1.66-2(c). In addition, transfers between the spouses for the benefit of their dependent children will not be considered a transfer of earned income for purposes of I.R.C. § 66(a). *Id.* In *Rutledge v. Commissioner*, 63 T.C.M. (CCH) 1926 (1992), *aff’d without op.* (5th Cir. 1993), the Tax Court also determined that there is no transfer of earned income deposited in a joint account over which the earning spouse had sole control and from which the other spouse did not make any withdrawals. Relief under I.R.C. § 66(a) was denied, however, in a case in which the spouse seeking relief had ready access to and withdrew her husband’s earned income from a joint account. *Drummer v. Commissioner*, 67 T.C.M. (CCH) 2963 (1994).

If all the requirements of I.R.C. § 66(a) are satisfied, then any community income for the calendar year is treated in accordance with the allocation rules in I.R.C. § 879(a). These rules override usual community property allocations, with the following results:

1. Earned income is treated as the income of the spouse who rendered the personal services.
2. Trade or business income is treated as the income of the person exercising substantially all the management and control of the trade or business.
3. A partner’s distributive share of partnership income is treated as the income of the partner.

4. Income derived from separate property is treated as the income of the spouse who owns the property.
5. All other community income is treated as provided in the applicable state community property law.

If the requirements of I.R.C. § 66(a) cannot be satisfied because, for example, the couple did not live apart for the entire taxable year, a spouse may be relieved of liability with respect to an item of community income under I.R.C. § 66(b). This provision permits the IRS to disallow the income-splitting benefits of community property law to a spouse for any income, if the spouse acted as if he or she were solely entitled to the income and failed to notify his or her spouse of the nature and amount of the income before the due date (including extensions) for filing a return for the taxable year in which such income was reportable. Whether a spouse has acted as if solely entitled to the income is a determination based on the facts and circumstances, with the focus on whether the income was used or made available by the spouse for the benefit of the marriage. Treas. Reg. § 1.66-3. If I.R.C. § 66(b) applies, such income will be included entirely in the gross income of the spouse who acted as if he or she were solely entitled to such income. Treas. Reg. § 1.66-3.

If a spouse does not otherwise qualify for relief under I.R.C. § 66(a) or (b), the IRS is authorized to provide equitable relief under I.R.C. § 66(c), which is the separate-return counterpart to the joint-return innocent-spouse relief provision (discussed in section 9.3, *supra*). For a requesting spouse to be eligible for such equitable relief, I.R.C. § 66(c) generally requires all the following:

1. The requesting spouse did not file a joint return for the taxable year for which relief is requested.
2. The requesting spouse did not include in his or her gross income for the taxable year an item of community income otherwise properly includible, which under the rules of I.R.C. § 879(a) would be treated as the income of the nonrequesting spouse.
3. The requesting spouse establishes that he or she did not know of, and had no reason to know of, the item of community income.



4. Taking into account all facts and circumstances, it would be inequitable to include the item of community income in the requesting spouse's gross income for reporting purposes.

I.R.C. § 66(c); Treas. Reg. § 1.66-4.

If all these conditions are satisfied, then the item of community income will be included in the gross income of the nonrequesting spouse and not in the gross income of the requesting spouse. Moreover, even if all the conditions cannot be met because, for example, the requesting spouse knew of the income, I.R.C. § 66(c) authorizes the IRS to provide equitable relief if, taking into account all the facts and circumstances, it would be inequitable to hold the requesting spouse liable.

The key distinctions between I.R.C. § 66(c) and I.R.C. § 66(a) are that I.R.C. § 66(c) eliminates the requirements that the spouses live apart, that at least one of the spouses have earned income, and that there be no transfers of such earned income between the spouses. In addition, I.R.C. § 66(c) adds a general requirement that the spouse requesting relief not know—or have reason to know—of the unreported item of community income (although the IRS is authorized to provide equitable relief even if the requesting spouse had knowledge of such income). The regulations under I.R.C. § 66 set forth similar factors for assessing a requesting spouse's knowledge of unreported income as the regulations that apply to innocent spouse cases. *See* Treas. Reg. § 1.66-4(a)(2); *supra* § 9.3.

The regulations under I.R.C. § 66 also make clear that in evaluating whether it is inequitable to include the unreported community income in the gross income of the spouse seeking relief, relevance will be attached to whether the requesting spouse significantly benefitted, directly or indirectly, from the unreported income. For these purposes, a *significant benefit* means any benefit received by the requesting spouse in excess of normal support. Treas. Reg. § 1.66-4(a)(3). Additional guidance on the circumstances under which equitable relief will be granted under I.R.C. § 66(c) is provided in Revenue Procedure 2003-61, 2003-32 I.R.B. 296. *See also Innocent Spouse Relief*, IRS Publ'n 971, available at <http://www.irs.gov/pub/irs-pdf/p971.pdf> (revised Apr. 2008).

The ability of the IRS to provide equitable relief under I.R.C. § 66(c), even in cases in which the requesting spouse may have had some knowledge of the unreported income, is especially important in a community property state because a concerned spouse cannot be

protected by simply filing a separate return. This is because, in a community property state, a spouse who files a separate return is still liable for the tax on one-half of the other spouse's community income. Therefore, I.R.C. § 66(c) serves to shield innocent spouses in community property states from being unfairly penalized for improper reporting on the part of a spouse.

In contrast to I.R.C. § 66(a) and (c), I.R.C. § 66(b) applies when a spouse is denied all information about the nature and amount of the other spouse's income and the uncooperative spouse also acts as if he or she were solely entitled to that income. If the uncooperative spouse files a return reporting only half of the community income, it may be possible for the aggrieved spouse to invoke I.R.C. § 66(b), in effect denying the uncooperative spouse the benefits of community property income reporting, particularly income splitting. The result is that the uncooperative spouse alone would be taxed on all the income earned or received. The problem, of course, is that the spouse earning or receiving the income can avoid tax liability on half the income merely by notifying the other spouse of the nature and amount of the income in a timely manner. There is no requirement that the income be shared with the nonearning or nonrecipient spouse. Consequently, the nonearning or nonrecipient spouse might receive notice of the community income but receive no funds with which to pay the resulting tax on his or her one-half share.

In Wisconsin, the nonearning or nonrecipient spouse may have remedies to deal with these problems. For example, a spouse in this position may have a claim against the other spouse for breach of the section 766.15 duty of good faith. Wis. Stat. § 766.70(1). Alternatively, the spouse may request an order for an accounting of the couple's property (including marital property income) and obligations, and may obtain a court order with respect to his or her ownership rights in, and access to, the marital property income. Wis. Stat. § 766.70(2). See sections 8.18 and 8.20, *supra*, for a detailed discussion of these remedies.

Separated spouses who are in the process of a divorce and are filing separate tax returns are particularly prone to fail to communicate important information needed to prepare their tax returns. Each spouse, however, is obligated to report one-half of all items of marital property income, absent a marital property agreement to the contrary. Increasingly, divorce courts are ordering spouses to share information about their income and deductions so that both can prepare accurate and

complete income tax returns. Without such an order, however, the tax law provides a spouse who is denied information no means to obtain the necessary information from payors, tax authorities, or tax return preparers.

Under I.R.C. § 6051(a), every employer who pays for services performed by an employee, or who is required to deduct and withhold FICA and income taxes from an employee, must furnish the employee with a statement (Form W-2) on the remuneration and withholding. In addition, payors of remuneration for services, dividends, corporate earnings and profits, gross proceeds received on behalf of a customer by a broker, interest, royalties, qualified-plan benefits, and a host of other items are required to file information returns (Form 1099 or a variant) about the payment of such amounts to any person. *See* I.R.C. §§ 6041–6050N. Similar information disclosure (Schedule K-1 or its equivalent) is required for distributions to partners, beneficiaries of estates and trusts, and shareholders of an S corporation. *See* I.R.C. §§ 6031, 6034A, 6037. Thus, in theory, ample documentation exists to permit a spouse who has been denied information by the income recipient to prepare his or her income tax return.

The difficulty lies in the fact that stringent confidentiality rules preclude disclosure of the necessary information. For example, I.R.C. § 6103(a) generally provides that returns and return information are confidential. The term *return information* clearly encompasses all the information required on a form W-2, Form 1099, Schedule K-1, or the like. *See* I.R.C. § 6103(b)(2). I.R.C. § 6103(a) prohibits the disclosure of return information by officers or employees of the United States, state and certain local agencies, and other persons who have obtained this information from a federal, state, or local agency, or an officer or employee of such an agency. While I.R.C. § 6103(e) does, for an individual income tax return, permit disclosure to persons having a “material interest,” the statutory list of such persons does not include the spouse or former spouse of a person filing separately. In addition, I.R.C. § 7216 makes it a misdemeanor for a tax-return preparer to unlawfully disclose return information. Therefore, it is clear that the IRS, the Wisconsin Department of Revenue (DOR), and tax-return preparers should not disclose to an inquiring spouse any information about the other spouse’s earnings, withholdings, or other income. Because no federal statute authorizes or compels an employer or payor to disclose income information to anyone other than the employee, payee, or beneficiary, no authority allows an employer or payor to furnish this

information directly to a separated spouse or a former spouse without the employee or payee's consent.

➤ **Practice Tip.** An individual who is not receiving cooperation from his or her estranged or former spouse in preparing an accurate income tax return should consider filing a separate return reporting all the income he or she has actually received and attaching a statement to the return advising the IRS that he or she is subject to community income reporting, but is unable to obtain information about his or her spouse's income. Such a disclosure may help establish the spouse's claim for innocent spouse relief under I.R.C. § 66(b) or (c). The disclosure may also help mitigate penalties in the event such relief is denied by the IRS.

A spouse seeking relief under I.R.C. § 66 must file Form 8857 within two years of the first collection activity by the IRS. Treas. Reg. § 1.66-4(j). Similar to the relief provisions under I.R.C. § 6015 for joint returns (*see supra* § 9.3), the IRS must send a notice upon its receipt of Form 8857 to the nonrequesting spouse informing him or her of the requesting spouse's request for relief. Treas. Reg. § 1.66-4(k).

From a procedural standpoint, it is important to note that the Tax Court has concluded that it does not have the jurisdiction to review a "stand alone" challenge to a denial for relief under I.R.C. § 66(c) in cases in which the requesting spouse failed to timely seek a review of the underlying deficiency determination. *Bernal v. Commissioner*, 120 T.C. No.6 (2003). In reaching its decision, the court pointed out that I.R.C. § 6015(e) specifically provides for a stand-alone proceeding, whereby an individual can petition the Tax Court in response to an adverse determination from the IRS for equitable relief with respect to a joint return without having to timely challenge the underlying deficiency. Conversely, I.R.C. § 66 does not specifically grant the Tax Court jurisdiction over the denial of equitable relief for a spouse filing a separate return in a community property state. Therefore, because the taxpayer in *Bernal* did not timely challenge the IRS's deficiency determination, the Tax Court had no jurisdiction to consider the denial of relief under I.R.C. § 66. The Tax Court did confirm, however, that it may review the denial of a spouse's request for relief under I.R.C. § 66 as part of a timely commenced deficiency proceeding.

## 2. Filing Separate Returns [§ 9.6]

When spouses file a joint federal income tax return, the characterization of income as marital or separate is usually unimportant. If the spouses file separate income tax returns, however, the characterization and classification of income becomes an important issue.

The IRS has published instructions explaining how income and deductions are to be allocated when spouses residing in a community property state file separate tax returns. See *Community Property*, IRS Publ'n 555, at <http://www.irs.gov/pub/irs-pdf/p555.pdf>. The DOR has also published guidance on how Wisconsin's marital property law affects married persons who file separate returns. See *Tax Information for Married Persons Filing Separate Returns and Persons Divorced in 2009*, Wisconsin Department of Revenue Publ'n 109 [hereinafter DOR Publ'n 109], available at <http://www.dor.state.wi.us/pubs/pb109.pdf>. The general rule is that income is allocated between spouses in accordance with applicable state law. One notable exception is that state community property laws will not apply to IRA distributions, which are instead taxable solely to the IRA owner and reported only on his or her separate tax return. I.R.C. § 408(d); *Morris v. Commissioner*, 83 T.C.M. 1104 (2002); *Bunney v. Commissioner*, 114 T.C. 259 (2000).

In Wisconsin, all income from marital property assets, and all income from individual property and predetermination date property assets for which no unilateral statement under section 766.59 has been executed, is classified as marital property pursuant to section 766.31(4). This income should be divided equally between the spouses for purposes of filing separate income tax returns. Deductions relating to the production of marital property income also should be divided equally between the spouses. Presumably, this rule also holds true for expenses incurred to produce income from individual property or predetermination date property assets for which no unilateral statement has been executed, since that income also is treated as marital property. Deductions relating to the production of separate (nonmarital property) income are deductible by the spouse who owns the income, provided that the deductions are paid from his or her nonmarital property funds. Expenses that are not attributable to any specific income, such as medical expenses, are deductible by the spouse who pays them unless they are paid with marital property funds, in which case they are divided equally between the spouses. Capital gains and losses on individual property or

predetermination date property assets, as well as expenses attributable to such assets, ordinarily are allocable to the spouse who owns the asset that gives rise to the gain or loss. If there is a marital property component to the gain by virtue of section 766.63(2), then apportionment of the gain may be required. *See supra* ch. 3. Each spouse may claim one-half of income taxes withheld on income that is classified as marital property. Treas. Reg. § 1.31-1(a).

Revenue Ruling 87-13, 1987-1 C.B. 20, holds that, in the absence of a marital property agreement, Wisconsin spouses filing separate returns each must report 50% of the marital property income received by either spouse as long as they are married. The only other possible exception to the requirement of community property reporting would be the innocent-spouse provisions of I.R.C. § 66(a), (b), or (c), discussed in section 9.4, *supra*, if applicable to one of the spouses. These rules provide equitable relief from community property reporting requirements in certain instances to achieve fairness.

One practical problem that arises when spouses file separate tax returns is that the one-half of their combined wages and other marital property income reported on their respective separate returns will not corroborate with the Form W-2 and Form 1099 information reported to the IRS with respect to such income. To forestall an inquiry from the IRS, spouses filing separate tax returns should attach an allocation worksheet to their respective returns showing how they calculated the income, deductions and income tax withheld reported by each of them. Examples of such allocation worksheets are included in IRS Community Property Publication 555, at <http://www.irs.gov/pub/irs-pdf/p555.pdf>, and in DOR Publication 109, *supra*. The allocation worksheet should be attached to each spouse's separate return and should document both what the spouse is reporting on the return and what will be reported by the other spouse. In addition, the worksheet should include an explanation that the filer is domiciled in Wisconsin and is reporting income under the community property rules.

Spouses filing separate tax returns need to exercise particular care in claiming estimated tax payments. Specifically, if estimated tax payments are filed in the name and tax identification number of only one spouse, the other spouse cannot receive credit for any part of the payment if the spouses file separate tax returns. *Janus v. United States*, 557 F.2d 1268 (9th Cir. 1977). This is true even if marital property funds are used for the estimated tax payments. This treatment of estimated tax payments

potentially could have harsh results, because a spouse may be required to report half the couple's marital property income and yet be unable to claim half the estimated tax payments made with respect to such income.

If spouses file a joint declaration of estimated tax and file separate returns, they may allocate the payments in any consistent manner that they may agree upon. If they cannot agree, the payment should be allocated in proportion to the tax liability reported on the returns as follows:

$$\frac{\text{Separate tax liability}}{\text{Both tax liabilities}} \times \text{Estimated Tax Payment}$$

Rev. Rul. 80-7, 1980-1 C.B. 296, *amplified by* Rev. Rul. 87-52, 1987-1 C.B. 347.

Revenue Ruling 87-13, 1987-1 C.B. 20, recognizes that the Act permits Wisconsin spouses to alter their property rights by marital property agreement, with at least prospective consequences for the tax treatment of their income if they file separate returns. For example, the IRS will recognize for federal income tax reporting purposes the validity of a marital property agreement that provides that any future income earned by either spouse for personal services will be the individual property of the earning spouse, rather than the marital property income of both spouses. It is even possible for a marital property agreement to provide that a percentage of what otherwise would be marital property income will be considered individual property. The IRS, however, does not permit allocation of more than one-half of the marital property income to the nonearning spouse. The IRS also will not recognize retroactive reclassification agreements, meaning that a marital property agreement will not be effective to change the character of income that has already been received or earned from marital property to individual property. *See Federal and Wisconsin Income Tax Reporting Under the Marital Property Act*, Wisconsin Dep't of Revenue Publ'n No. 113, at 15 [hereinafter DOR Publ'n 113].

➤ **Note.** Although published by the DOR, the content of DOR Publication 113 is a joint effort by the DOR and the Milwaukee office of the IRS. Specifically, in the publication the "federal treatment" reflects the interpretation of the Act by the IRS Milwaukee office, and therefore should be regarded as an authoritative statement of the

position of the IRS. The publication is available online at <http://www.dor.state.wi.us/pubs/pb113.pdf>.

As a general rule, divorcing spouses separately report one-half of the community property income for the portion of the year of the divorce during which they are still married. *See supra* § 9.4; *see also* I.R.C. § 6013(d)(2). A detailed discussion of the income-reporting rules for divorcing spouses is found in *Tax Information for Divorced or Separate Individuals*, IRS Publ'n 504. For a discussion of using marital property agreements and related planning techniques to avoid income allocation problems in the year when the divorce becomes final, see section 9.7, *infra*.

### **C. Federal Income Tax: Gain or Loss Transactions Between Spouses [§ 9.7]**

Generally, the transfer of property between spouses during marriage or incident to a divorce is a nontaxable event under I.R.C. § 1041. If a transfer is within the scope of I.R.C. § 1041(a), nonrecognition treatment is mandatory, even if the parties are acting at arms' length and the transferee spouse gives full consideration for the transferred property. Temp. Treas. Reg. § 1.1041-1T(a), Q&A-2 (1984). Therefore, spouses cannot sell property to each other to generate a taxable gain. The converse is also true under I.R.C. § 267(a), which prohibits claiming a taxable loss from the sale or exchange of property between spouses.

The rules under I.R.C. § 1041(a) are relatively straightforward. Specifically, gain or loss generally is not recognized on a transfer of property from an individual to, or in trust for, a spouse or a former spouse if the transfer is incident to a divorce. I.R.C. § 1041(a). The statute defines a transfer to be incident to a divorce if made within one year after the date the marriage ceases or if related to the cessation of the marriage. I.R.C. § 1041(c).

According to Temporary Treasury Regulation § 1.1041-1T(a), Q&A-5, a transfer of property between former spouses occurring not more than one year after the marriage ceases is subject to section 1041 treatment, even if the property transferred was acquired by the transferor after the divorce. Moreover, as long as the transfer between the former spouses occurs not more than one year after the marriage ceases, it does not have to be related to the cessation of the marriage. Temp. Treas. Reg.



§ 1.1041-1T(a), Q&A-6. A transfer of property between former spouses will be treated as related to a cessation of the marriage, however, only if the transfer is pursuant to a divorce or separation instrument and occurs not more than six years after the date on which the marriage ceases. Temp. Treas. Reg. § 1.1041-1T(b), Q&A-7. If the transfer occurs more than six years after the marriage ceases, section 1041 treatment will apply only if it can be shown that the transfer was made to effect the division of property owned by the parties at the time of the divorce and the delay was caused by factors impeding an earlier transfer, such as a valuation dispute or business impediment. *Id.*; *see* Priv. Ltr. Rul. 200221021 (May 24, 2002) (holding that court-ordered transfer of stock that took place more than six years after divorce is related to cessation of the marriage because delay resulted from compelling business reasons, including desire to maintain investor confidence, enhance stock value, and facilitate future growth).

Since a transfer of property between spouses or former spouses incident to divorce is a nonrecognition transaction, the property in the hands of the transferee is treated as if acquired by gift, with the result that the basis of the transferee is the adjusted basis of the transferor. I.R.C. § 1041(b). Under I.R.C. § 1223(2), the transferee of any carry-over basis property (including property transfers subject to I.R.C. § 1041) includes in his or her holding period the period during which the transferor spouse held the property. Because the disposition of property by gift does not trigger depreciation recapture under I.R.C. §§ 1245 and 1250, a transfer of property subject to I.R.C. § 1041 will not result in recapture. The transferee, however, will step into the transferor's shoes with respect to the recapture potential of the transferred property and could trigger a recapture by changing the use of the transferred property (for example, a change from business to personal use). *See* Temp. Treas. Reg. § 1.1041-1T(d), Q&A-13.

The nonrecognition rule of I.R.C. § 1041(a) does not apply if the spouse or former spouse of the transferor is a nonresident alien. I.R.C. § 1041(d). In addition, I.R.C. § 1041(e) provides for the recognition of gain on a transfer that would otherwise be nontaxable under I.R.C. § 1041(a) if the transfer is in trust for the transferee spouse and the liabilities assumed by the trust or encumbering the transferred property exceed its adjusted basis. Any gain recognized under I.R.C. § 1041(e) is added to the transferee trust's carry-over basis in the property transferred. Similarly, I.R.C. § 453B(g) requires the acceleration and recognition of gain on a section 1041 transfer of an installment

obligation into a trust. A direct transfer of an installment obligation between spouses or former spouses incident to divorce, however, will not be a taxable event under I.R.C. § 453B(g).

The nonrecognition rule of section 1041 has been construed to cover certain transfers of property made by one spouse (the *transferor spouse*) on behalf of a former spouse (the *nontransferor spouse*) to a third party. Specifically, Temporary Treasury Regulation § 1.1041-1T(c), Q&A-9, provides that there are three situations in which a transfer of property to a third party on behalf of a former spouse will qualify under section 1041 (provided all other requirements of the statute are met): (1) if the transfer to the third party is required by the qualified divorce or separation instrument; (2) if the transfer is pursuant to the written request of the nontransferor spouse; or (3) if the transferor spouse receives a written consent or ratification of the third party transfer from the nontransferor spouse. Under Q&A-9, a transfer of property made to a third party on behalf of a spouse is treated first as a deemed transfer of the property made directly to the nontransferor spouse in a transfer to which section 1041 applies, and then as a deemed transfer of the property from the nontransferor spouse to the third party in a taxable transaction to which section 1041 does not apply.

Uncertainty over what criteria should apply in determining the *on behalf of* standard in Q&A-9 has generated considerable litigation and confusion over how a corporate redemption of a spouse's stock in a transaction incident to a divorce should be treated for tax purposes. See *Read v. Commissioner*, 114 T.C. 14 (2000) (holding that stock redemption in connection with divorce will be nontaxable to the transferring spouse if (1) the transfer satisfied an obligation of the nontransferor spouse; (2) the transfer was *in the interest of* the nontransferor spouse; or (3) in making the transfer, the transferor spouse was acting as representative of the nontransferor spouse); *Craven v. United States*, 215 F.3d 1201 (11th Cir. 2000), *aff'g* 70 F. Supp. 2d 1323 (N.D. Ga. 1999) (holding that wife's transfer of her stock was on behalf of husband, because (1) wife was redeeming stock pursuant to couple's divorce settlement, (2) husband guaranteed the corporation's note to the wife, and (3) in guarantee, husband acknowledged terms were of direct interest, benefit, and advantage to him); *Arnes v. United States*, 981 F.2d 456 (9th Cir. 1992) (holding that wife not required to recognize gain on corporation's redemption of her half of community property stock pursuant to divorce agreement, because transfer was really on behalf of husband, who was required to bear burden of tax on gain recognized as

result of redemption). In general, if a corporation buys stock from a spouse in a transaction incident to a divorce, the payment of the redemption proceeds will be considered a constructive distribution to the nontransferor spouse if the corporation is deemed to be satisfying a legal obligation of the nontransferor spouse to the transferor spouse. In such situations, the gain realized on the redemption is taxable to the nontransferor spouse as if he or she had received the redemption proceeds (rather than to the transferor spouse who actually received the payment from the corporation)

In 2003, the IRS issued final regulations designed to provide greater certainty and flexibility to divorcing spouses regarding the tax treatment of stock redemptions incident to divorce. Treas. Reg. § 1.1041-2. These regulations provide that divorcing spouses can agree in their divorce agreement as to which spouse should bear the tax consequences of the redemption. Specifically, the divorcing spouses have the option of treating the redemption as resulting in a constructive distribution to the nontransferor spouse, and therefore, taxable to the nontransferor spouse. Conversely, the spouses can agree in their divorce agreement that the redemption will be taxable to the transferor spouse who actually receives the redemption proceeds, even though under applicable tax law the redemption would otherwise result in a constructive distribution to the nontransferor spouse whose legal obligation has been satisfied. The spouses can elect to use these special rules by specifying their mutual intent in a divorce agreement concerning whether the redemption should be treated as a distribution to the transferor spouse or the nontransferor spouse. The divorce agreement must also document the spouses' agreement to file their income tax returns in a manner consistent with such intent. In addition, the divorce agreement must expressly supersede any other agreement between the spouses concerning the redemption of the stock.

➤ **Practice Tip.** To avoid any uncertainty or unintended consequences with respect to the redemption of stock incident to a divorce, the spouses' divorce agreement should specify which spouse will bear the tax consequences of the redemption. The agreement should be drafted to comply with the requirements of Treasury Regulation § 1.1041-2. Absent such an agreement, a stock redemption incident to divorce could trigger an unintended and unexpected constructive dividend to the nontransferor spouse.

Because transfers of property between former spouses incident to a divorce are nontaxable carry-over basis events under I.R.C. § 1041, the impact of future capital gains taxes should be considered in the context of the parties' negotiations over property division. Specifically, if one spouse receives mostly assets with significant unrealized appreciation and a low carry-over basis and the other spouse receives mostly assets with a high carry-over basis, the negative impact of capital gains taxes on the first spouse when the assets are ultimately disposed of may be substantial. Under section 767.61(3)(k), a Wisconsin divorce court may consider the tax consequences to each party as one of the factors that may permit deviation from the statutory presumption of equal division of property upon divorce.

Although I.R.C. § 1041(a) provides that no gain or loss is recognized on a transfer of property between spouses and former spouses incident to a divorce, it may not operate to prevent the taxability of income that is assigned by reason of a transfer of the underlying asset (for example, accrued interest on transferred bonds and certificates of deposits or dividends on transferred stock). Until recently, the IRS had taken the position that although I.R.C. § 1041(a) shields gains that would ordinarily be recognized on a transfer of property from recognition, it does not shield income that is ordinarily recognized upon the assignment of that income to another taxpayer. Instead, the historic position of the IRS has been that such income remains taxable to the transferor spouse without regard to I.R.C. § 1041.

The IRS first stated its position on the assignment-of-income doctrine in the context of transfers incident to a divorce in Revenue Ruling 87-112, 1987-2 C.B. 207. In this ruling, the IRS concluded that I.R.C. § 1041 did not apply and that under assignment-of-income principles the transferor spouse must include the deferred accrued interest on Series E and EE bonds in gross income under I.R.C. § 454 in the year such bonds were transferred to the transferor's former spouse incident to their divorce. Under I.R.C. § 454 and Treasury Regulation § 1.454-1(a), the accrued interest on Series E and EE bonds is not includible in gross income until the taxable year in which the bond matures, is redeemed, or is disposed of, whichever is earlier, unless the taxpayer elects to report the interest income as it accrues. The ruling also provided that the nontransferor spouse's basis in the bonds must be increased by the amount of accrued interest recognized by the transferor spouse.

Until recently, the IRS had also taken the position that retirement benefits and deferred compensation arrangements not covered by specific statutory exceptions, such as nonqualified deferred-compensation plans, were taxable to the transferor spouse under assignment-of-income principles. *See* Field Serv. Advisory, FSA 200005006 (Feb. 4, 2000) (contradicted by Rev. Rul. 2002-22, 2002-1 C.B. 849). In Revenue Ruling 2002-22, 2002-1 C.B. 849, however, the IRS reversed its position on the assignment of income doctrine versus the applicability of I.R.C. § 1041. According to Revenue Ruling 2002-22, a spouse who transfers interests in nonstatutory stock options and nonqualified deferred compensation to his or her former spouse incident to divorce does not recognize income on the transfer by reason of I.R.C. § 1041. Instead, the nontransferor spouse must include an amount in gross income when he or she exercises the stock options or when the deferred compensation is paid or made available to that spouse. The IRS restricted the ruling, however, so that it does not apply to transfers of nonstatutory stock options, unfunded deferred-compensation rights, or other future income rights to the extent that such options or rights are not vested at the time of transfer or to the extent that the transferor spouse's rights to the income are subject to substantial contingencies at the time of transfer.

The IRS expanded upon Revenue Ruling 2002-22 in Revenue Ruling 2004-60, 2004-24 I.R.B. 1, in which it ruled that the transfer of interests in nonstatutory stock options and in nonqualified deferred compensation from the employee spouse to the nonemployee spouse incident to a divorce does not result in payment of wages for FICA and FUTA tax purposes. These interests are, however, subject to FICA and FUTA tax when exercised by the nonemployee spouse to the same extent as if the options or right to compensation had been retained and exercised by the employee spouse.

The IRS has clarified the scope of Revenue Ruling 2002-22 in several private letter rulings. Specifically, in Private Letter Ruling 200646003 (Aug. 7, 2006), the IRS ruled that income attributable to the exercise of nonstatutory stock options that were transferred by an employee to his former spouse pursuant to a property settlement agreement incident to a divorce in a community property state was includible in the gross income of the nonemployee spouse. The employee continued to hold the options after the divorce but was legally required to comply with his former spouse's written instructions to exercise the options. When he received such instructions, he exercised the options, immediately sold the stock, and forwarded the proceeds to his former spouse. The IRS ruled that all

income realized from the exercise of the options and the subsequent sale of the stock was reportable by the former spouse, notwithstanding the fact that the employee earned the options in connection with his performance of services. This ruling is significant because it specifically extends the holdings in Revenue Rulings 2002-22 and 2004-60 to taxpayers in community property states.

In Private Letter Ruling 200519011 (Jan. 13, 2005), the IRS, citing Revenue Ruling 2002-22, concluded that the division of nonstatutory and statutory stock options between divorcing spouses pursuant to a property settlement agreement is made for full and adequate consideration and is not taxable as a gift.

In Private Letter Ruling 200442003 (June 22, 2004), the IRS concluded that the assignment-of-income doctrine did not apply to a husband's lump-sum payment to his ex-wife in return for her transferring to him her community property interest in his supplemental executive retirement plan (SERP), a nonqualified employee-benefit plan. Accordingly, neither husband nor wife was required to include any amount in their gross income with respect to the transfer.

Under the facts of this ruling, the divorce judgment awarded the wife a one-half community property interest in the husband's SERP and she was to receive a pro rata portion of each payment made to husband from the SERP after his retirement. Several years after the divorce judgment, the husband reached the age of eligibility for retirement at his company, but elected not to retire. Accordingly, no amounts were yet payable under the SERP. The wife wanted to start receiving her one-half share of the benefits under the SERP and filed an action seeking an order requiring husband to buy out her interest in the SERP. The parties eventually reached a settlement, and the husband agreed to pay the wife a lump sum in return for her release of her rights under the SERP.

The IRS, citing Revenue Ruling 2002-22, ruled that the transfers constituted transfers between spouses incident to divorce within the meaning of I.R.C. § 1041 and that the assignment-of-income doctrine did not apply. The IRS further ruled that the transfers were for full and adequate consideration and did not result in a taxable gift by either the husband or wife to the other.

Revenue Ruling 2002-22 directly addresses the question of assignment of income versus section 1041, and signaled a dramatic

reversal of the historic position of the IRS on this issue. The ruling contains a section entitled “Prospective Application” and appears to have an impact beyond the taxation of nonqualified stock options and deferred compensation. Specifically, the ruling includes a statement that Revenue Ruling 87-112, *supra*, “is clarified by eliminating references to assignment of income principals” (Revenue Ruling 87-112 was reaffirmed, however, respecting the application of I.R.C. § 454 to the transfer and the determination of the nontransferor spouse’s basis).

➤ **Note.** Surprisingly, the IRS limited Revenue Ruling 2002-22 to divorce transactions and specifically stated that the ruling does not apply to transfers of property between spouses not in connection with a divorce. This position is puzzling, because I.R.C. § 1041 makes no such distinction and applies to both marital transfers and transfers in connection with divorce.

In addition to Revenue Ruling 2002-22, the Internal Revenue Code includes a number of provisions specifically addressing the tax treatment of divorce-related transfers and distributions of qualified plan benefits and other deferred retirement benefits to nonowner and nonparticipant spouses that have the effect of superseding both I.R.C. § 1041 and the assignment-of-income rules. For example, I.R.C. § 408(d)(6) provides that the transfer of an individual’s interest in an IRA to a former spouse under a divorce agreement is not treated as a taxable transfer and the nontransferor spouse is to be considered the owner of the account for tax purposes. *See* Treas. Reg. § 1.408-4(g)(1). *But see* *Bunney v. Commissioner*, 114 T.C. 259 (2000) (holding that distribution from IRA funded with community funds to account-holder husband, who subsequently transferred portion of distributed funds to former wife pursuant to community property division, was taxable to husband); *Czepiel v. Commissioner*, 78 T.C.M. (CCH) 378 (1999) (holding that taxpayer who took distributions from his IRA to pay ex-wife amounts owed to her under divorce agreement was not considered to have transferred an “interest” in the IRA under I.R.C. § 408(d)(6), because divorce agreement only required that money be paid to wife, not that an interest in IRA be transferred to her).

➤ **Note.** A complex set of rules, the discussion of which is beyond the scope of this chapter, also applies to the assignment and taxation of qualified plan benefits at divorce. *See, e.g.*, I.R.C. §§ 401(a)(13),

414(p) (setting forth statutory requirements for qualified domestic relations orders (QDROs) assigning qualified plan benefits).

The nonrecognition rule of I.R.C. § 1041 also does not apply to certain property received by the transferee spouse that represents the right to receive income, such as accounts receivable and interest on installment obligations. The nontransferor spouse generally cannot invoke I.R.C. § 1041 to avoid the recognition of income upon receipt of such payments. For example, in *Cipriano v. Commissioner*, 81 T.C.M. (CCH) 1856 (2001), the Tax Court rejected the taxpayer's contention that installment payments denominated as interest represented postdivorce appreciation in the value of her former husband's law practice and should be treated as nontaxable transfers of property under I.R.C. § 1041. The ex-wife had been awarded a lump-sum amount, payable in installments, plus interest, for her equitable interest in her ex-husband's law practice. The Tax Court concluded that the payments designated as interest compensated the ex-wife for the delay in her receipt of her share of the marital assets to which she was entitled as of the day of the divorce, and therefore constituted interest income. *See also Gibbs v. Commissioner*, 73 T.C. Memo. (CCH) 2669 (1997) (rejecting ex-wife's argument that interest portion of cash settlement paid to her in installments was excludable under I.R.C. § 1041 as received in exchange for property transferred to ex-husband incident to divorce).

In *Balding v. Commissioner*, 98 T.C. 368 (1992), however, the IRS unsuccessfully argued that a series of settlement payments received by an ex-wife pursuant to a divorce decree modification in exchange for the release of her claim to a possible community property interest in her ex-husband's retirement pay gave rise to taxable income. The Tax Court rejected the IRS's contention that receipt of the settlement payments should be characterized as income, rather than as a nontaxable event under I.R.C. § 1041. *See also Newell v. Commissioner*, T.C. Summary Op. 2003-1, 2003 WL 57921 (U.S. Tax Court Jan. 7, 2003) (payments taxpayer received from her former spouse's military retirement plan were excludable from her gross income as a property settlement.).

➤ **Practice Tip.** In many cases, the most valuable assets acquired during a marriage are IRAs, deferred compensation, qualified retirement benefits, and other employment benefits. The impact of future income taxes on these assets must be considered in the context of the spouses' negotiations over property division. In addition, a spouse who receives payments under an installment note in



connection with the property division should be advised that the interest received on the note will be taxable as ordinary income and will not be excludable under I.R.C. § 1041.

#### **D. Federal Income Tax: Payment of Maintenance or Alimony from Community Earnings [§ 9.8]**

Payments constituting alimony or separate maintenance are included in the gross income of the payee spouse under I.R.C. § 61(a)(8) and I.R.C. § 71(a) and are deductible under I.R.C. § 215(a) in computing the payor spouse's adjusted gross income. Because alimony and maintenance payments are deducted in computing adjusted gross income (i.e., an above-the-line deduction), the payor spouse can claim the alimony deduction even if he or she uses the standard deduction. Under I.R.C. § 71(b), a payment constitutes alimony or separate maintenance when: (1) the payment is made in cash; (2) the payment is received by or on behalf of the payee spouse under a divorce or written separation agreement; (3) the spouses are divorced or legally separated and they reside in separate households when the payment is made; (4) payments to a third party on behalf of the payee spouse are evidenced by a timely writing; (5) the payor spouse's liability to make the payment does not continue for any period after the payee spouse's death; (6) the payor and payee (if married) do not file a joint return; and (7) the divorce or separation agreement does not designate nonalimony treatment.

A potential problem has long existed in community property states with respect to decrees of separate maintenance or written separation agreements requiring that payments be made by one spouse to the other spouse during the period between their separation (but while they are still married) and the entry of the divorce judgment. The problem is essentially one of double taxation. Under I.R.C. § 61, one-half of community earned income is taxable to each spouse, even though the nonearner spouse may receive none or only a small part of that income. At the same time, I.R.C. § 71 requires the spouse who has no earned income to include alimony or separate maintenance payments in his or her gross income. The Tax Court has prevented double taxation under these circumstances by not applying I.R.C. § 71 to separate maintenance payments that were significantly less than the nonearning spouse's taxable share of community earnings. On the other hand, the nonearning spouse must report one-half of the community income on his or her separate return, even though the alimony or separate maintenance

payments he or she receives are significantly less than his or her share of the community income. *Id.* If the alimony or separate maintenance payments exceed the payee spouse's share of current community income, such amounts are taxable to the payee spouse as alimony and deductible by the payor spouse. *Furgatch v. Commissioner*, 74 T.C. 1205 (1980); *see also* Rev. Rul. 62-115, 1962-2 C.B. 23; Rev. Rul. 74-393, 1974-2 C.B. 28.

## **E. Federal Income Tax: Special Provisions Regarding Community Income or Community Property [§ 9.9]**

### **1. In General [§ 9.10]**

A number of specific provisions in the Internal Revenue Code deal with community property. These provisions generally negate the income-splitting consequences of community ownership and, particularly in the case of earned income, attribute it to the party who performs the services or activities that generate the income. Among the areas affected are those discussed in section 9.11–.16, *infra*.

### **2. Earned Income Credit [§ 9.11]**

Under I.R.C. § 32(c)(2)(B)(i), a person's earned income is computed without regard to any community property laws in determining the availability of the earned income credit. In this manner, income is ascribed to its earner rather than divided equally between the earner and the earner's spouse.

### **3. IRAs [§ 9.12]**

Under I.R.C. § 219(f)(2), community property laws are disregarded for purposes of administering maximum contribution rules for IRAs. Similarly, under I.R.C. § 408(g), community property laws are disregarded for purposes of determining the tax treatment of IRA distributions.

Despite I.R.C. § 408(g), state community property laws are given effect when classifying or partitioning IRAs. In several private letter

rulings involving Wisconsin taxpayers, the IRS has ruled that the reclassification by marital property agreement of one spouse's IRA as marital property, and the partition by agreement of one spouse's marital property IRA into equal shares thereafter held by the spouses as separate property, would not cause a taxable distribution from the IRA pursuant to I.R.C. § 408(d)(1). Significantly, in each case, no part of the IRA balance was actually transferred from the spouse holding the account into an IRA maintained on behalf of the other spouse during the account-holder spouse's lifetime, and no distributions from the IRA were made to the nonaccount-holder spouse during the account-holder spouse's lifetime. Instead, the transfer was accomplished strictly by reclassification of the IRA under a marital property agreement. Priv. Ltr. Rul. 9419036 (May 13, 1994); Priv. Ltr. Rul. 9439020 (Sept. 30, 1994).

The postdeath partition of a Wisconsin marital property IRA also has been held not to constitute a taxable distribution under I.R.C. § 408(d)(1). Priv. Ltr. Rul. 9427035 (July 8, 1994). Under the facts of this ruling, the decedent's IRA account had been classified as marital property by the terms of a marital property agreement. The decedent designated his revocable trust as the beneficiary of the IRA. The trust allocated the surviving spouse's marital property interest in the IRA to a survivor's trust created under the decedent's revocable trust. The survivor's trust was fully revocable by the surviving spouse, and the surviving spouse did in fact revoke the trust shortly after the decedent's death. Because of the intervention of the two trusts (the decedent's revocable trust and the survivor's trust), there was a concern that the distribution of the surviving spouse's marital property share of the IRA through the survivor's trust to the surviving spouse would not qualify for tax-free rollover treatment under I.R.C. § 408(d)(3). The specific question was whether the surviving spouse would be treated as having acquired the IRA distribution from a third party, rather than from the decedent, the consequence of which would be to deprive the surviving spouse of the ability to accomplish a tax-free rollover of the distribution into her own IRA. The ruling (and a number of others that have followed) is significant in its holding that in situations in which the surviving spouse has the power to revoke the trust receiving the survivor's share of a marital property IRA, the general rule about IRA distributions in trust will not apply, and the IRS will treat the surviving spouse as having acquired the IRA directly from the decedent and not from the trust. Accordingly, the surviving spouse will be treated as a direct beneficiary of a 50% interest in the decedent's IRA, thereby permitting the surviving spouse to roll over such interest tax-free into an

IRA in his or her own name. *See also* Priv. Ltr. Rul. 200304037 (Jan. 24, 2003); Priv. Ltr. Rul. 199925033 (June 25, 1999).

The IRS reached a much different result in Private Letter Ruling 199937055 (Sept. 17, 1999). Under the facts of this ruling, a Wisconsin married couple proposed to sever the husband's IRA, which was classified as marital property pursuant to a marital property agreement, into two separate equal shares and, during the husband's lifetime, actually transfer one-half of the IRA to a new IRA established by the wife in a direct custodian-to-custodian transfer. This new IRA would be classified as the wife's individual property pursuant to the couple's marital property agreement, and her children would be named primary beneficiaries. Moreover, it was proposed that distributions from the new IRA would be made to the wife during her lifetime based on her and her oldest child's joint life expectancies, and that distributions would commence on the date specified in the agreement.

The primary question posed by the taxpayers in Private Letter Ruling 199937055 was whether the actual severance of the husband's IRA and distribution of the wife's one-half share in the IRA to her own separate IRA during the husband's lifetime would be considered a taxable distribution. Unfortunately for the taxpayers, the IRS emphatically answered this question in the affirmative. Before reaching this decision, the IRS first confirmed that I.R.C. § 408(g) does not abrogate any of a spouse's substantive rights under state law and agreed that a spouse may have a marital property interest in an IRA to the extent the existence of that interest is consistent with state law. The IRS also confirmed that the reclassification of an IRA as marital property pursuant to a marital property agreement is not considered a taxable distribution for purposes of I.R.C. § 408(d)(1), because such reclassification alone is not tantamount to an actual distribution or payment from the IRA. The IRS ruled, however, that an actual transfer of the wife's marital property interest in the husband's IRA to her own IRA would constitute a taxable distribution under I.R.C. § 408(d)(1). In reaching this conclusion, the IRS stated as follows:

The owner of an IRA account is deemed to be the individual in whose name the account was established. This conclusion is not affected by state law. In any event, even if title does not determine ownership under applicable state law, and even if the IRA owner's spouse's property interests in the IRA are identical to the owner's under applicable state law, distributions from the IRA are to be taxed as if the owner is the sole owner of the IRA.

Based on Private Letter Ruling 199937055, the clear position of the IRS is that, even if a spouse is considered the owner of one-half of an IRA under state community or marital property laws, distributions from the IRA are to be taxed pursuant to I.R.C. § 408(d) to the account holder as if the account holder is the sole owner of the IRA. Two recent U.S. Tax Court decisions appear to support this result. See *Morris v. Commissioner*, 83 T.C.M. (CCH) 1104 (2002); *Bunney v. Commissioner*, 114 T.C. 259 (2000) (holding that state community property laws will not apply to IRA distributions taxable to IRA owner under I.R.C. § 408(d) and reported only on his or her separate tax return).

#### **4. Self-employment Taxes [§ 9.13]**

There are no unique problems created for Wisconsin spouses with regard to self-employment taxes if joint returns are filed. When separate returns are filed, however, a determination must be made as to which spouse is liable for the self-employment tax.

Even though the income that generates a self-employment tax liability may be classified as marital property, and therefore should be split by the spouses, the attendant self-employment tax is imposed on only one of the spouses. Under I.R.C. § 1402(a)(5)(A), in determining the net earnings from self employment that are subject to the self-employment tax, community income from a trade or business is treated as follows: all the gross income and deductions attributable to a trade or business (other than a trade or business carried on as a partnership) are generally treated as belonging to the spouse carrying on the trade or business. If the trade or business is jointly operated, the gross income and deductions are attributed to each spouse on the basis of their respective distributive share of the gross income and deductions. If the self-employment tax liability is generated by income from a partnership, the spouse who is the partner is liable for the self-employment tax, even if a portion of the partner's distributive share of income or loss is marital property and is taxable to the other spouse. I.R.C. § 1402(a)(5)(B); Treas. Reg. § 1.1402(a)-8(b).

If both spouses are partners, the self-employment tax is allocated based on their distributive share. Treas. Reg. § 1.1402(a)-8(b).

## 5. S Corporation Election [§ 9.14]

The election by the shareholders of a qualifying small business corporation to be an S corporation under I.R.C. §§ 1361–1379 requires the consent of all shareholders. I.R.C. § 1362(a). When S corporation stock is owned by a husband and wife as community property, or when the income from the stock is community property, both spouses must consent to the election. Treas. Reg. § 1.1362-6(b)(2)(i). A husband and wife, however, are treated as one shareholder under I.R.C. § 1361 for purposes of the rule limiting the number of shareholders in an S corporation to 100. I.R.C. § 1361(c)(1). This rule applies whether the stock is held by each spouse individually or in some form of joint ownership. Treas. Reg. § 1.1361-1(e)(2).

The income rule in section 766.31(4) classifies the income from individual property and predetermination date property as marital property (i.e., community property), at least when no unilateral statement under section 766.59 has been executed. Accordingly, the previously discussed S corporation election requirements have particular significance in Wisconsin for S corporation stock holdings that are the individual property or predetermination date property of one spouse. Unless the owner spouse has executed a unilateral statement classifying the income from the stock as his or her individual property, both spouses must join in the execution of an S corporation election.

The courts have upheld the two-signature requirement for S corporation elections involving S corporation stock owned as community property, despite contrary state management and control rules. In *Seely v. Commissioner*, 51 T.C.M. (CCH) 1087 (1986), the husband alone had signed the S corporation election form, allegedly relying on his wife's oral consent to act on her behalf. Even though the signatures of both spouses were not required by California law for management and control of community property, the court rejected the idea that the husband alone could act for the couple in making an S corporation election, stating that the two-signature requirement was one of federal tax law and not state property law. *See also Clemens v. Commissioner*, 453 F.2d 869 (9th Cir. 1971), *aff'd* 28 T.C.M. (CCH) 1225 (1969); *Forrester v. Commissioner*, 49 T.C. 499 (1968) (involving a separate, but untimely, election by the second spouse).

Under Revenue Procedure 2004-35, I.R.B. 2004-23, automatic relief is given for late filing of shareholder consents for spouses of S

corporation shareholders in community property states if the S corporation election is invalid solely because (1) Form 2553 (Election by a Small Business Corporation) failed to include the signature of a community property spouse who is a shareholder solely pursuant to state community property law, and (2) both spouses have reported all items of income, gain, loss, deduction, or credit consistent with the S corporation election on all affected income tax returns.

An S corporation election by a United States resident spouse was ineffective in a situation in which the other spouse was a nonresident alien and had a community property interest in the corporation's stock under the laws of Mexico, which disqualified the corporation from S corporation eligibility because, under I.R.C. § 1361, nonresident aliens are not permitted to be shareholders in an S corporation. *Ward v. United States*, 661 F.2d 226 (Ct. Cl. 1981).

If a shareholder dies before consenting to an S corporation election, the personal representative of the deceased shareholder's estate may file the necessary consents on behalf of both the deceased shareholder and his or her estate. Rev. Rul. 92-82, 1992-2 C.B. 238. Presumably, the reasoning of Revenue Ruling 92-82 also applies in cases in which S corporation stock is owned as community property and would permit the personal representative of a spouse who dies before signing the required consent to execute the consent on the deceased spouse's behalf.

## **6. Disregarded Entities [§ 9.15]**

A single-member limited liability company (LLC) that does not elect to be taxed as a corporation will be treated as a sole proprietorship for tax purposes if the member is an individual. Treas. Reg. § 301.7701-2(a). The ability to disregard the LLC as a separate entity for tax purposes provides the opportunity for the owner of the LLC to achieve nontax objectives, such as liability protection, without the added burden of having to prepare and file separate partnership tax returns as would normally be required for an LLC. Instead, the member can simply report the LLC's income, losses, and other tax items on the member's individual income tax return.

The IRS has ruled that an LLC that is owned solely by a husband and wife as community property may be treated as having a single owner and disregarded as a separate entity for tax purposes. Rev. Proc. 2002-69,

2002-2 C.B. 831. Under Revenue Procedure 2002-69, a general partnership or limited partnership that is owned solely by a husband and wife as community property may also be treated as having only a single owner and be disregarded as a separate entity for tax purposes. Alternatively, Revenue Procedure 2002-69 provides that if for some reason spouses who are the sole owners of an LLC or partnership elect to treat the entity as a partnership for federal tax purposes and file appropriate partnership tax returns, the IRS will accept that the entity is a partnership for tax purposes.

In Private Letter Ruling 200339026 (June 23, 2003), the IRS also ruled that an LLC that is wholly owned under state law by a revocable trust established by spouses residing in a community property state will be treated as a disregarded entity for federal tax purposes.

## **7. Distributions in Complete Redemption of Stock Owned as Community Property [§ 9.16]**

Under certain circumstances, spouses owning corporate stock as community property may partition their holdings and have one of the spouses subsequently make a redemption of his or her stock under I.R.C. § 302. Under I.R.C. § 302(a), if a corporation redeems its stock and if subsection (1), (2), (3), or (4) of I.R.C. § 302(b) applies to the redemption, the redemption is treated as a distribution in part or full payment in exchange for the stock, thus avoiding treatment of the distribution as a dividend. Under I.R.C. § 302(b)(3), exchange treatment under I.R.C. § 302(a) applies to a redemption if it is a complete redemption of all the corporation's stock owned by the shareholder. Under I.R.C. § 302(c)(1), the constructive ownership rules of I.R.C. § 318(a) are made applicable to transactions under I.R.C. § 302, with the result that an individual is considered as owning stock owned by or for his or her spouse or child. *See* I.R.C. § 318(a)(1).

Under certain conditions, spelled out in I.R.C. § 302(c)(2)(A), the constructive ownership rules of I.R.C. § 318(a)(1) are deemed not to apply in determining whether a redemption completely terminates a shareholder's interest. These conditions are that (1) immediately after the distribution the distributee has no interest in the corporation (including an interest as an officer, director, or employee) other than an interest as a creditor, (2) the distributee does not acquire any such interest (other than stock acquired by bequest or inheritance) within 10



years from the date of such distributions, and (3) the distributee files an agreement to notify the IRS of any acquisition described in clause (2) above and to retain necessary records. Further qualifications of these exceptions are found in I.R.C. § 302(c)(2)(B). These qualifications generally nullify the I.R.C. § 302(c)(2)(A) three-point exception to the constructive ownership rules if, within the 10-year period preceding the date of distribution, the distributee acquired any part of the redeemed stock from a person whose ownership of stock would be attributable to the distributee, or if the distributee transferred stock to such a person within the 10-year period. The purpose of these provisions is to prevent shifts in proportionate stock ownership between redeeming and nonredeeming family members immediately before a complete redemption of stock is carried out.

In the context of such a complete redemption, it was held that the partition of a husband and wife's community property stock into separate, equal holdings in the names of the husband and of the wife, followed by redemption of only the husband's shares, met the requirements of a complete termination of interest under I.R.C. § 302(b)(3). Rev. Rul. 82-129, 1982-2 C.B. 76. Revenue Ruling 82-129 specifically held that the partition did not result in an acquisition (or transfer) of stock for purposes of I.R.C. § 302(c)(2)(B), because neither spouse owned any more stock after the partition than they owned before.

In Wisconsin, a "partition" of the sort described in Revenue Ruling 82-129 apparently would have to be accomplished by a marital property agreement reclassifying one-half of the total number of marital property shares as the individual property of each spouse and by having new certificates issued for the reclassified shares. *See* Wis. Stat. § 766.31(10). This is because no specific judicial procedure exists for partition of marital property between the spouses during the marriage, absent extraordinary circumstances. *See, e.g.,* Wis. Stat. § 766.70.

In another ruling that involved a complete termination of interest, Rev. Rul. 71-138, 1971-1 C.B. 109, it was held that in a situation in which 50% of the stock in the corporation was owned by a husband and wife as community property, and the remaining 50% was owned by their son, a redemption of the community property stock of the husband and wife would meet the requirements of a complete termination of interest under I.R.C. § 302(b)(3) and the attribution rules of I.R.C. § 318(a)(1) would not apply if both the husband and wife filed the distributee

agreement with the IRS as required by clause (iii) of I.R.C. § 302(c)(2)(A).

More recently, in Private Letter Ruling 199942018 (Oct. 22, 1999) the husband's entire stock ownership interest was redeemed. Following the husband's redemption, his wife continued her employment with the corporation. The couple resided in a community property state and, to prevent the wife's salary from being considered a prohibited retained interest of the husband for purposes of I.R.C. § 302, the couple entered into a property agreement that provided that all consideration paid to the wife in her capacity as an employee of the corporation would be classified as her sole and separate property. The IRS ruled that a complete redemption of the husband's interest in the corporation had occurred, subject to the validity of the property agreement that all earnings paid to his wife will be her sole and separate property.

➤ **Note.** At least for the moment, the distinction between dividend and exchange treatment for stock redemptions is largely moot, because the Jobs and Growth Tax Relief Reconciliation Act of 2003, (JGTRRA), Pub. L. No. 108-27, 117 Stat. 752, effectively reduced the tax rate on dividends to be the same as the tax rate applicable to capital gains. Specifically, JGTRRA added I.R.C. § 1(h)(11), which taxes an individual's "qualified dividend income" as net capital gain. *Qualified dividend income* generally refers to dividends received from domestic corporations and from certain foreign corporations. There has been considerable speculation that the qualified dividends rules may eventually be repealed and that the ordinary income tax treatment applicable to dividends in effect before JGTRRA will again apply. But such repeal has not yet occurred.

## **F. Federal Income Tax: Income Tax Issues Following Death [§ 9.17]**

### **1. Treatment of Income from Community Property [§ 9.18]**

The long-standing rule of federal income taxation is that following the death of one of the spouses, one-half of the income from the community property is taxed to the decedent's estate, and the other half to the surviving spouse. *United States v. Merrill*, 211 F.2d 297 (9th Cir.

1954); *Grimm v. Commissioner*, 89 T.C. 747 (1987), *aff'd*, 894 F.2d 1165 (10th Cir. 1990). Under sections 861.01 and 857.01, a personal representative in Wisconsin succeeds to ownership of only the decedent's undivided one-half interest in marital property assets at the time of death, and thus the aforementioned rule applies for purposes of allocating income between the decedent's estate and the surviving spouse. In the case of survivorship marital property assets, however, which pass at the death of one spouse by operation of law to the surviving spouse through a nontestamentary disposition, all the postmortem income from the property is taxed to the surviving spouse.

The personal representative of a decedent's estate may elect to file a joint return with the surviving spouse covering the decedent's income during the portion of the year preceding the date of death. I.R.C. § 6013(a)(3). A joint return may not be filed, however, if the surviving spouse has remarried before the close of the taxable year in which the death occurred or if the surviving spouse is a nonresident alien. I.R.C. § 6013(a). If the personal representative is concerned about avoiding the joint and several liability that results under I.R.C. § 6013(d)(3) from filing a joint return, a separate final return should be filed for the decedent. Regardless of whether a joint or a separate return is chosen, income in respect of a decedent cannot be reported on the decedent's final return, but must be reported on the income tax return of the estate, entity, or person receiving the income. I.R.C. § 691(a). Deductions in respect of a decedent are handled similarly. I.R.C. § 691(b).

Difficult questions arise following the death of one of the spouses concerning the treatment of postmortem income from marital property assets held by a revocable trust created by only one of the spouses. The property classification and management and control aspects of this situation are discussed in sections 10.60–.63, *infra*. Although there is no authority on the subject, it appears that if the settlor spouse dies first, the trustee should report the income attributable to the decedent's interest in property as the income of an irrevocable trust, and treat the income attributable to the surviving spouse's interest in former marital property assets as the income of a grantor trust, at least until expiration of the limitation period for the surviving spouse to commence an action to recover his or her share of former marital property assets under section 766.70(6)(b)1. Conversely, if the nonsettlor spouse dies first, the trustee should continue to treat the income from the settlor's property interests as the income of a grantor trust and treat the income from the former

marital property interest of the deceased nonsettlor spouse as income payable to that spouse's estate.

## 2. Forced and Voluntary Estate Planning Elections

### [§ 9.19]

A decedent spouse may attempt to dispose of both halves of community property via a testamentary forced-election estate plan. If the surviving spouse acquiesces and permits all the community property to be subject to probate administration (or permits its transfer to a revocable trust) so that both halves pass in conjunction with the forced-election estate plan, the surviving spouse nevertheless will continue to be taxed on the income attributable to his or her share of marital property assets during the period of administration. *Wells Fargo Bank & Union Trust Co. v. United States*, 245 F.2d 524 (9th Cir. 1957).

Other important postmortem income tax consequences follow from a surviving spouse's acquiescence to a forced election that subjects his or her half of community assets to the estate plan under the decedent spouse's will. In such cases, the courts have treated the election as an exchange by the surviving spouse of a remainder interest in his or her half of the community property for an income interest in the decedent's half of the community property. *Estate of Christ v. Commissioner*, 480 F.2d 171 (9th Cir. 1973), *aff'g* 54 T.C. 493 (1970); *Gist v. United States*, 423 F.2d 1118 (9th Cir. 1970); *Kuhn v. United States*, 392 F. Supp. 1229 (S.D. Tex. 1975). Because in a forced election the survivor has in effect purchased a wasting asset (i.e., a life estate in the decedent's half of the community property), the survivor was historically entitled to amortize the cost basis over his or her life expectancy. *Estate of Christ*, 480 F.2d 171; *Gist*, 423 F.2d 1118. The amortization deduction is now barred, however, by I.R.C. § 167(e) unless the remaindermen are not related to the survivor. To the extent that the amortization deduction is available, it effectively offsets the amount of income received from the deceased spouse's half of the community assets, rendering that part of the trust income tax-free to the survivor for all intents and purposes.

It should be noted that the IRS has not taken a formal position on the income tax consequences of the forced spousal election to the deceased spouse's estate or trust, although an exchange of property of some sort has taken place. It has been suggested that the receipt of a remainder interest in the surviving spouse's share of community property in

exchange for an income interest in the decedent's share of community property might be deemed to be a one-time assignment of ordinary income subject to tax. *Kuhn v. United States*, 392 F. Supp. 1229, 1238 (S.D. Tex. 1975); *see also Commissioner v. P.G. Lake, Inc.*, 356 U.S. 260 (1958).

Another problem is presented by I.R.C. § 1001(e), which provides that if a life estate in property, an interest in property for a term of years, or an income interest in trust is sold or otherwise disposed of, the portion of the adjusted basis of the interest acquired by inheritance, gift, or nonrecognition interspousal transfer is disregarded in determining gain or loss. If this section applies in the context of a forced election, the deceased spouse's estate or trust may have no basis in the life estate it transfers in exchange for the remainder interest of the surviving spouse and thus may be forced to recognize gain on the consideration received from the surviving spouse. The amount realized is probably limited to the lesser of the actuarial value of the remainder interest received from the surviving spouse or the actuarial value of the life estate transferred to the surviving spouse.

The serious income tax consequences that attend a forced-election estate plan contrast with the general absence of such problems in a voluntary election estate plan. In a voluntary election estate plan, because the surviving spouse is entitled to an income interest in the deceased spouse's half of the community property, regardless of whether the surviving spouse places his or her half of the community property in trust, there is no sale or exchange.

Both forced-election and voluntary-election estate plans involve federal estate tax and federal gift tax issues. *See infra* §§ 9.63, .73, .96; *see also infra* ch. 10.

### **3. Exchanges of Former Marital Property Assets After Death of One Spouse [§ 9.20]**

For probate purposes, the Act uses the item-by-item rule instead of the aggregate rule. Wis. Stat. § 861.01. Under the item-by-item rule, after the death of one spouse the surviving spouse owns an undivided one-half interest in each item of former marital property. Therefore, after the death of one spouse the surviving spouse and the beneficiaries

of the deceased spouse will own the former marital property assets as tenants in common.

In many cases, the surviving spouse and the beneficiaries will want to exchange their undivided interests among themselves so that each person owns an entire asset. If so, the question arises whether such a transaction is a taxable exchange for federal and Wisconsin income tax purposes. Of course, if marital property assets receive a full adjustment in basis under I.R.C. § 1014(b)(6), any gain recognized on an exchange after the death of one spouse would be limited to appreciation occurring after the spouse's death. Therefore, I.R.C. § 1014(b)(6) may mitigate, but not eliminate, the capital-gains consequences of a taxable exchange.

In Revenue Ruling 69-486, 1969-2 C.B. 159, the IRS held that a taxable exchange occurred between two beneficiaries of a trust. In that ruling, the terms of the trust instrument required the trustee to distribute one-half of the trust assets to A and the other one-half to B. At the time of termination, the trust owned notes with a value of 300x dollars and common stock with a value of 300x dollars. Although the notes and common stock had the same fair market value, the trust's basis in the notes was different from its basis in the stock. At the request of the beneficiaries, the trustee distributed the notes to A and the common stock to B. At the time of distribution, A and B received assets of equal value. The IRS ruled that there was a taxable exchange between the beneficiaries, stating the following:

Since the trustee was not authorized to make a non-pro rata distribution of property in kind, but did so as a result of the mutual agreement between A and B, the non-pro rata distribution by the trustee to A and B is equivalent to a distribution to A and B of the notes and common stock pro rata by the trustee, followed by an exchange between A and B of A's pro rata share of common stock for B's pro rata share of notes.

In subsequent rulings, the IRS has confirmed that Revenue Ruling 69-486 requires gain recognition when a trustee makes a non-pro rata distribution to beneficiaries based upon their agreement and no independent authority to do so exists under state law or the governing trust instrument. *See* Priv. Ltr. Rul. 9429012 (July 22, 1994); Priv. Ltr. Rul. 9424026 (June 17, 1994). *But see* Priv. Ltr. Rul. 200334030 (May 19, 2003) (no gain recognized as a result of non-pro rata distributions of property under plan of termination when will was silent on whether non-pro rata distributions could be made, but such distributions were

permitted under state law). These rulings, however, did not involve a division of community property with a surviving spouse.

In Revenue Ruling 76-83, 1976-1 C.B. 213, the IRS ruled that an equal, but non-pro rata, division of community property by two spouses under a divorce property settlement agreement was not a taxable exchange. In subsequent rulings outside of the divorce context, the IRS has confirmed that an equal non-pro rata division of community property between living spouses is not an income taxable event. *See* Priv. Ltr. Rul. 8003109 (Oct. 26, 1979); Priv. Ltr. Rul. 8037124 (June 23, 1980). In several rulings, the IRS has extended the holding of Revenue Ruling 76-83 to the equal non-pro rata division of community property after the death of one spouse. *See* Priv. Ltr. Rul. 199925033 (June 25, 1999); Priv. Ltr. Rul. 199912040 (Mar. 26, 1999); Tech. Adv. Mem. 8505006 (Oct. 19, 1984); Priv. Ltr. Rul. 8016050 (Jan. 23, 1980). Perhaps significantly, however, in each of the rulings involving the division of community property after the death of one spouse, either the terms of the governing trust instrument or applicable state law expressly authorized the trustee to make non-pro rata distributions of property.

The IRS has not ruled on whether it would extend the holding of Revenue Ruling 76-83 to a non-pro rata division of community property after the death of one spouse in cases in which neither the applicable state law nor the deceased spouse's estate planning documents expressly authorize such a non-pro rata division. Previously this created some uncertainty for Wisconsin attorneys, because Wisconsin law formerly did not expressly grant a personal representative or trustee the power to make non-pro rata distributions amongst beneficiaries.

In response to this uncertainty, 2005 Wisconsin Act 216 created new section 766.31(3)(b), which now allows spouses to provide in a marital property agreement that at the death of the first spouse to die some or all their marital property may be divided based on aggregate value rather than item by item. Wis. Stat. § 766.31(3)(b)1. In addition, a surviving spouse and the successor in interest to the deceased spouse's share of marital property may enter into an agreement that provides that some or all of the marital property in which each has an interest will be divided based on aggregate value rather than item by item. Wis. Stat. § 766.31(3)(b)2. For this purpose, a *successor in interest* includes any person or entity that succeeds to the marital property interest of the deceased spouse including, for example, a personal representative, a trustee, or the beneficiary of a nonprobate transfer. Committee Note to

2005 Wis. Act 216, § 42. (For details about the Committee Notes, see section 2.22, *supra*.) In the absence of such a provision in a marital property agreement or in an agreement between a surviving spouse and a successor in interest, the item-by-item system will apply.

Under section 766.31(3)(b)3., a surviving spouse and a distributee who is a successor in interest to all or part of a deceased spouse's interest in marital property may petition the court to approve an exchange of interests in marital property authorized by an agreement described in subdivision 766.31(3)(b)1. or 2. Court approval of the exchange, however, is not required for such an agreement to be effective.

An exchange of former marital property interests between a surviving spouse and a distributee of the decedent spouse under section 766.31(3)(b) will be treated as a nontaxable exchange for Wisconsin income tax purposes. *See* Wis. Stat. § 71.05(6)(a)16., (b)(12).

➤ **Practice Tip.** It is good practice to specify in a married couple's estate planning documents that the personal representative and trustee have the authority to make non-pro rata distributions of marital property after the death of the first spouse to die. The couple's estate planning documents should also specifically provide that the personal representative and the trustee have the authority to enter into agreements with the surviving spouse providing for the non-pro rata division of marital property.

#### **4. Depreciation, Depletion, and Amortization of Former Marital Property Following Death of One Spouse [§ 9.21]**

As a general rule, under I.R.C. § 167(a) a depreciation deduction is allowed for exhaustion and wear and tear of property used in a trade or business or of property held for the production of income. The modified accelerated cost recovery system (MACRS) depreciation rules of I.R.C. § 168 apply to certain types of property. I.R.C. § 167(b).

For I.R.C. § 167 depreciation purposes, the basis upon which the exhaustion, wear and tear, and obsolescence is to be measured is the adjusted basis of the property under I.R.C. § 1011 for purposes of determining the gain or loss on sale or disposition of the property. I.R.C.



§ 167(c). In turn, I.R.C. § 1011 refers to the cost or other basis of property, determined under I.R.C. § 1012 “or other applicable sections of this subchapter.” This would include the provisions of I.R.C. § 1014(b)(6), which, following the death of one of the spouses, grants both the decedent’s and the surviving spouse’s halves of community property a full adjustment in basis. *See infra* § 9.24. Accordingly, following the death of one of the spouses, both halves of former marital property assets should qualify for depreciation using their newly adjusted basis for property depreciable under I.R.C. § 167. *See, e.g.*, Priv. Ltr. Rul. 9326043 (July 2, 1993) (giving basis adjustments under I.R.C. § 1014(b)(6) to both decedent’s and surviving spouse’s community property interests in literary copyrights and permitting interests to be depreciated under I.R.C. § 167 over remaining useful life of copyrights).

Similar rules also apply to community property consisting of working and royalty interests in oil and gas property following the death of one spouse for which cost (but not percentage) depletion is allowable under I.R.C. §§ 611–612. *See* Rev. Rul. 92-37, 1992-1 C.B. 195 (on joint return covering decedent’s short taxable year and surviving spouse’s 12-month taxable year, surviving spouse’s cost-depletion allowance attributable to her share of former community property oil and gas interests was calculated using her basis at end of taxable year, which included basis adjustment under I.R.C. § 1014(b)(6)).

If former marital property is depreciable under I.R.C. § 168 using the MACRS, the depreciation method applicable to the surviving spouse’s adjusted basis depends on when the property was originally placed in service. Theoretically, this could result in the one-half interest in the former marital property acquired by the surviving spouse from the deceased spouse and the surviving spouse’s own one-half interest in such property being subject to different depreciation methods, because the MACRS is applicable only to property placed in service after 1986 (property placed in service after 1980 and before 1987 is depreciable under the former accelerated cost recovery system (ACRS) and property placed in service before 1981 is not eligible for accelerated cost recovery). Specifically, for MACRS depreciation purposes, the one-half interest in the former marital property received by the surviving spouse from the deceased spouse will be deemed to have been placed in service as of the date of the deceased spouse’s death, but the one-half interest in the property already owned by the surviving spouse will be deemed to have been placed in service as of the date the property was originally placed in service by the couple. Therefore, the one-half interest owned

by the surviving spouse in the former marital property will not be eligible for MACRS treatment if the property was placed in service before 1987. *See Estate of Grassier v. Commissioner*, 93 T.C. 236 (1989) (holding, in case in which married couple placed depreciable community property assets in service before 1981, because each spouse had present equal interests in property from time it was acquired and had placed property in service before 1981, the surviving spouse's one-half interest was not eligible to use ACRS).

➤ **Example.** Husband and wife acquire and place in service depreciable property in 1986. The property is held as survivorship marital property. The husband dies in 2003. Although the entire property will receive a new basis under I.R.C. § 1014(b)(6), the depreciation method applicable to each half of the property will be different. The half of the property that the wife inherits from her husband is considered to be placed in service in 2003 and is eligible for the MACRS. However, the half of the property that the wife owned when the property was acquired is treated as being placed in service in 1986. This half is not eligible for the MACRS, but can be depreciated using the ACRS. *See DOR Publ'n 113, supra* § 9.6, at 31.

Similar rules apply to the amortization of intangible property under I.R.C. § 197, which permits certain intangibles such as goodwill and going-concern value acquired after August 10, 1993, to be amortized over a 15-year period. Specifically, for I.R.C. § 197 amortization purposes, the one-half interest in intangible property received by the surviving spouse from the deceased spouse will be deemed to have been acquired as of the date of the deceased spouse's death and will be amortizable regardless of whether the property was acquired by the couple before August 10, 1993, but the one-half interest in the intangible property already owned by the surviving spouse as his or her marital property share will be deemed to have been acquired as of the date the intangible property was originally acquired by the couple. Therefore, the one-half interest owned by the surviving spouse in the intangible property will not be amortizable under I.R.C. § 197 if the property was acquired by the couple before August 10, 1993. *See Priv. Ltr. Rul. 199949037* (Dec. 10, 1999) (holding that because married couple acquired intangible property before August 10, 1993, interest in such property acquired by surviving spouse from her husband as result of his death was amortizable under I.R.C. 197, but her own one-half

community property interest in such intangible property was not amortizable).

## **5. Treatment of Proceeds of Life Insurance Policies Owned by Deferred-employment-benefit Plans [§ 9.22]**

Under section 766.61(8), the various time-based apportionment rules in section 766.61 for determining the property law classification of life insurance policies are made inapplicable to a policy held by a deferred-employment-benefit plan. The statute further provides that the classification of deferred employment benefits, regardless of the nature of the assets held by the deferred-employment-benefit plan, is determined under section 766.62, which contains its own set of time-based apportionment rules for classifying deferred employment benefits and differs in a number of significant respects from section 766.61. *Compare* §§ 2.170, .197, *supra*.

It is significant that although the property law rules in Wisconsin treat life insurance contracts owned by deferred-employment-benefit plans the same as other assets of the plan are treated, the proceeds of life insurance policies are afforded special treatment for federal income and estate tax purposes. If the plan participant dies before retirement, and if the death benefit under the plan is payable from the proceeds of a life insurance policy, the difference between the cash surrender value and the face amount of the policy is treated as life insurance death proceeds for income tax purposes and is exempt from income taxation under I.R.C. § 101(a) to the extent that the cost of the insurance has been paid with nondeductible employee contributions or has been taxable to the employee. *See* Treas. Reg. § 1.72-16(c)(4). The balance of the proceeds, representing the cash surrender value of the policy, will be treated as a distribution from the plan and taxed accordingly. I.R.C. § 72(m)(3)(C); Treas. Reg. § 1.72-16(c). If the employee did not pay the cost of the life insurance protection and was not taxed on the cost of the life insurance protection, no part of the proceeds paid to the beneficiary is excludable under I.R.C. § 101(a).

With respect to death taxes, the proceeds of policies insuring the life of a deceased plan participant typically are includible in the participant's gross estate under I.R.C. § 2042 if the participant held any incidents of

ownership (such as the right to designate the beneficiary) at the time of death or if the proceeds are payable to the participant's estate.

## **G. Federal Income Tax: Basis-adjustment Rules for Community Property [§ 9.23]**

### **1. In General [§ 9.24]**

An important federal tax rule applicable to community property jurisdictions is the full adjustment to basis accorded to community property acquired from a decedent under I.R.C. § 1014(b)(6). That provision states that the surviving spouse's one-half share of community property held by the decedent and the surviving spouse "under the community property laws of any state" is considered to have been acquired from the decedent, if at least one-half of the whole of the community interest in the property was includible in determining the value of the decedent's gross estate for federal estate tax purposes. Because property acquired from a decedent takes either the fair market value as of the date of death or an alternate value under I.R.C. § 2032 as its basis under I.R.C. § 1014(a), this is an extremely significant provision that permits both spouses' halves of former community property to receive a basis adjustment at death. Significantly, this full-adjustment-to-basis rule is not accorded to common law forms of co-ownership such as joint tenancy with right of survivorship, tenancy by the entirety, or tenancy in common. Only one-half of property held in those forms of co-ownership is includible in the estate of a deceased cotenant; correspondingly, only that half is entitled to a basis adjustment under the rules of I.R.C. § 1014(a) and (b)(9). Pursuant to Treasury Regulation § 1.1014-2(a)(5), the filing of a federal estate tax return, or the payment of federal estate tax, is not necessary to obtain the special community property basis treatment.

It should be noted that I.R.C. § 1223(11) contains a companion rule on the holding period of assets acquired from a decedent. The statute accords long-term capital-gains treatment to both halves of community property receiving a basis adjustment under I.R.C. § 1014(b)(6), regardless of whether the property is disposed of within one year following a spouse's death.

Even though the full-basis-adjustment rule of I.R.C. § 1014(b)(6) is relatively simply stated, in application it has produced some interesting results in community property states. These are reviewed below.

## **2. No Basis Adjustment for Income in Respect of a Decedent [§ 9.25]**

Pursuant to I.R.C. § 1014(c), the general basis-adjustment rule of I.R.C. § 1014 does not apply to property that consists of the right to receive items of income in respect of a decedent (IRD) under I.R.C. § 691. As a result, it has been held that no adjustment to basis is available to a surviving spouse for an interest in an installment obligation attributable to a predeath sale of community property, because the installment obligation constitutes IRD. *Holt v. United States*, 39 Fed. Cl. 525 (1997); *Stanley v. Commissioner*, 338 F.2d 434 (9th Cir. 1964), *aff'g* 40 T.C. 851 (1963); Rev. Rul. 76-100, 1976-1 C.B. 123; *see also Estate of Cartwright v. Commissioner*, 71 T.C.M. (CCH) 3200 (1996) (holding that payments made by decedent's law firm to his estate for work in process were not paid solely to redeem his stock in the firm and were instead IRD that was not eligible for a basis step-up); Rev. Rul. 68-506, 1968-2 C.B. 332 (holding that benefits received by employee from an exempt employee's trust, half of which had been includible for estate tax purposes in deceased nonemployee spouse's estate, is IRD and not eligible for a basis step-up); Priv. Ltr. Rul. 20034-5026 (Nov. 7, 2003) (holding that neither deceased spouse's nor surviving spouse's interest in annuity contract held as community property was entitled to a stepped-up basis). Thus, at least one type of community property interest—namely, items that constitute IRD—is excluded from the full-adjustment-to-basis rule.

An approach related to the application of the I.R.C. § 1014(b)(6) full adjustment to basis is found in *Willging v. United States*, 474 F.2d 12 (9th Cir. 1973). In *Willging*, a husband and wife owned a grain farm as community property and had elected to report their income on the accrual basis. This involved adding to the sales price of products sold during the year the value of their closing inventory and subtracting the value of their opening inventory. During the taxable year of the husband's death, the opening inventory was small; on the date of his death, it was large. The court found that the husband's death constituted an event of realization that fixed the value of the closing-grain inventory for his half of the operation as of his date of death. The court rejected

the wife's argument that her share of the small opening-grain inventory should be adjusted to its date-of-death value so that she could escape ordinary income taxation on the difference between the value of the opening inventory and the comparatively large value at the time of death. Instead, the court held that the date of death was an event of realization under the accrual method of accounting for her as well as her deceased husband. Accordingly, the I.R.C. § 1014(b)(6) adjustment to basis simply was unavailable to the surviving spouse to shelter her half of the farm's ordinary income. It is not clear why the government did not choose to pursue this case as an IRD question under I.R.C. § 691, but the result seems correct and consistent with the installment obligation cases decided under I.R.C. § 1014(c). It is interesting to note that the result would have been different if the farm operation had been conducted on a cash basis, since the court made clear that both halves of the inventory would then have received a basis adjustment to their value on the date of death.

A full I.R.C. § 1014(b)(6) basis adjustment was granted in Private Letter Ruling 9829025 (July 17, 1998), which involved a married couple who entered into an exchange agreement and sold a parcel of community property real estate in a transaction that was intended to qualify for nonrecognition treatment as a like-kind exchange under I.R.C. § 1031. Before the replacement property could be identified, however, the husband died. Later, the replacement property was identified, and the exchange was completed. The IRS ruled that the exchange of properties qualified for nonrecognition treatment under I.R.C. § 1031, and therefore, the proceeds from the exchange attributable to the husband's interest in the property did not constitute IRD. The IRS further ruled that the deceased husband should be treated as owning one-half of the replacement property as of his date of death. Accordingly, his surviving wife was entitled to a full basis adjustment for the replacement property under I.R.C. § 1014(b)(6).

### **3. Basis Adjustment for Assets Characterized as Community Property by Agreement [§ 9.26]**

It appears well settled that state law determines the extent to which the spouses may use agreements to classify their property. The two decided cases on point—*Massaglia v. Commissioner*, 286 F.2d 258 (10th Cir. 1961), *aff'd* 33 T.C. 379 (1959), and *Crosby v. Commissioner*, 20 T.C.M. (CCH) 1422 (1961)—both involved taxpayers who had entered

into prior agreements converting their community property to separate property. These agreements were held to control under state law, thus denying the surviving spouse the benefit of the full adjustment in basis under I.R.C. § 1014(b)(6).

A number of revenue rulings issued by the IRS have specifically acknowledged that agreements valid under state law were effective to reclassify property and, at least prospectively, income. *See* Rev. Rul. 77-359, 1977-2 C.B. 24; Rev. Rul. 73-390, 1973-2 C.B. 12; Rev. Rul. 73-391, 1973-2 C.B. 12 (discussed in section 9.35, *infra*). While these revenue rulings purport to respect classifications by agreement for federal income tax purposes, none of them deal with or specifically mention the full-basis-adjustment rule of I.R.C. § 1014(b)(6). It should follow, however, that if the property laws of a state permit a reclassification of other property to community property (or to marital property in Wisconsin), then the reclassification should be given effect by the IRS for all relevant tax law purposes. The reclassification of property by marital property agreement, by gift, by conveyance, by life insurance consent (under section 766.61(3)(e)), or by unilateral statement (under section 766.59) is specifically authorized under section 766.31(10). It follows that a reclassification by any of these methods changing individual property or “other” property to marital property should control for federal tax purposes.

Decisions denying tax effect to the classification of community property by agreement under an elective system of community property appear to be inapplicable in Wisconsin, because the Act creates a system of community property dictated by state policy as an incident of matrimony. *See, e.g.,* Wis. Stat. § 766.001(2). The problem with agreements entered into under an elective system of community property is illustrated by *Commissioner v. Harmon*, 323 U.S. 44 (1944), in which the Supreme Court refused to permit the splitting of income between spouses who had elected to be governed by Oklahoma’s elective community property system (now repealed). The court distinguished between a legal (i.e., mandatory) system of community property, which automatically vests half of the income and assets of the community during marriage in each spouse, and an elective community property system, which is essentially consensual in nature. In holding that Oklahoma’s elective community property system was ineffective in splitting incomes for purposes of filing separate income tax returns, the Court grounded its decision in the underlying *nature* of the community

property system, rather than on the mere ability to alter property classifications by agreement.

In contrast to an elective system of community property, Wisconsin's system of marital property is a legal system of community property. *See supra* ch. 2. Under the Supreme Court's rationale in *Harmon*, the tax consequences of that characterization must be given effect.

In 1998, the state of Alaska enacted an elective community property system that purports to be available to both Alaska residents and out-of-state residents who contribute property to an Alaska community property trust. *See* Alaska Community Property Act, Alaska Stat. ch. 34.77 (West, WESTLAW current through legislation effective May 17, 2010 passed during the 2010 Second Regular Session of the 26th Legislature). The drafters of the Alaska community property legislation stated that property that is classified by a married couple as community property under Alaska's elective community property law will qualify for a full basis adjustment under I.R.C. § 1014(b)(6) upon the death of one spouse. The proponents of the legislation believed that the Supreme Court's distinction in *Harmon* between elective and legal systems of community property has largely been rendered moot since the filing of joint returns by married couples was authorized in 1948. They also argued that the expansion of the *Harmon* doctrine to the basis-adjustment area was unwarranted, and that the elective versus legal distinction should be limited to the assignment-of-income context.

The drafters of the Alaska community property law did not seek an official opinion from the IRS as to whether the proposed legislation would be respected as creating a community property interest for federal tax purposes, and the IRS has yet to rule on the issue. Therefore, it remains uncertain whether property classified as "community property" under Alaska's elective community property law will be treated as community property for federal tax purposes. Several comprehensive articles have been written describing Alaska's elective community property system. *See* David G. Shaftel & Stephen E. Greer, *Obtaining a Full Stepped-Up Basis Under Alaska's New Community Property System*, Estate Planning, Mar./Apr. 1999, at 109; Jonathan G. Blattmachr et al., *Tax Planning with Consensual Community Property: Alaska's New Community Property Law*, 33 Real Prop., Prob. & Trust J. 615 (1999).



#### **4. Basis Adjustment for Deferred Marital Property Assets [§ 9.27]**

The nature of each spouse's interest in deferred marital property is discussed in chapter 2, *supra*. Because the augmented deferred marital property election in section 861.02 operates only upon deferred marital property owned or retained at death by a deceased spouse, the interests of a spouse who owns deferred marital property at death will be completely different from the interests of a spouse who does not own such property.

With respect to the interest of the owner of probate assets that meet the definition of deferred marital property under section 851.055, that interest is a full ownership interest that extends up to and including the moment of death. It has been held that quasi-community property under the former California quasi-community property statute, section 201.5 of the California Probate Code, is fully includible in the decedent owner's gross estate for federal estate tax purposes, and that the interest of the surviving spouse is a mere expectancy. *Estate of Sbicca*, 35 T.C. 96 (1960). It follows that all of such property will receive a fully adjusted basis for federal income tax purposes under I.R.C. § 1014(b)(1). The former California quasi-community property statute bore considerable substantive similarity to section 851.055 and the former Wisconsin deferred marital property election under the prior version of section 861.02, and thus the same treatment should apply for deferred marital property that is probate property and is elected by the surviving spouse under the augmented deferred marital property election in section 861.02.

With respect to the interest of the owner of retained property rights in nonprobate deferred marital property assets that are included in the augmented deferred marital property estate for purposes of the election in section 861.02, no federal tax cases have been decided under the analogous provisions of California's revised quasi-community property statute, section 102 of the California Probate Code (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 21 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot). The deferred marital property interests included in the augmented deferred marital property estate under section 861.03(2), however, all appear to be includible in the federal gross estate of a deceased spouse under one or more of I.R.C. §§ 2036 to 2042. To the extent that such property

interests are includible in the gross estate of the deceased spouse under those provisions, they should receive a full adjustment in basis for federal income tax purposes under I.R.C. § 1014(b).

Viewed from the standpoint of the spouse who is not the owner, the deferred marital property interest has two aspects. Until the death of the owner, the interest of the surviving spouse in deferred marital property is at most a nonvested future elective right to take property, and not a vested property interest. The owner spouse continues to have the exclusive right of management and control of the property (consistent with the nature of his or her ownership interest) while both spouses are living. *See* Wis. Stat. § 766.51(6). If the owner spouse dies, the elective rights ripen and may be exercised by the surviving spouse, provided that the right to elect ceases with the subsequent death of the surviving spouse. Wis. Stat. § 861.09. If the nonowner spouse dies first, no elective rights exist. Accordingly, no deferred marital property interest would be includible in the gross estate of a predeceasing nonowner spouse for federal estate tax purposes, and no basis adjustment under I.R.C. § 1014(b)(6) would result.

## **5. Basis Adjustment for Community Property Converted to Other Forms of Ownership [§ 9.28]**

### **a. Joint Tenancy and Tenancy in Common Assets [§ 9.29]**

Only one-half of the value of joint-tenancy or tenancy-in-common assets owned by spouses is includible in the gross estate of the first spouse to die under I.R.C. § 2040(b). As a result, only the includible one-half interest, and not the entire property, is entitled to a basis adjustment at death under I.R.C. § 1014(b)(9). Conflicts over the availability of the full adjustment to basis under I.R.C. § 1014(b)(6) have arisen in cases in which marital property assets are intentionally reclassified by the agreement of the spouses into common law property, such as joint tenancy or tenancy in common.

In several instances, courts have held that the conversion of community property to common law property renders the property something other than “community property held by the decedent and the surviving spouse,” and the full adjustment in basis to both halves of the

property consequently has been denied. *Estate of Young v. Commissioner*, 110 T.C. 297 (1998) (holding that California real estate held in joint tenancy was not community property, despite determination by a local California probate court that it should be classified as community property); *Murphy v. Commissioner*, 342 F.2d 356 (9th Cir. 1965), *aff'g* 41 T.C. 608 (1964) (holding that California community property real estate converted to joint tenancy and then to tenancy in common was not community property for purposes of I.R.C. § 1014(b)(6)); *Bordenave v. United States*, 150 F. Supp. 820 (N.D. Cal. 1957) (holding that California real estate purchased with community property, but titled in joint tenancy, was rebuttably presumed to be joint tenancy under California law); Rev. Rul. 68-80, 1968-1 C.B. 348 (holding that New Mexico community property converted to Virginia tenancy in common was not entitled to basis step-up under I.R.C. § 1014(b)(6)).

In cases in which there are no state property law rules concerning the classification of property held in joint tenancy, the result may be different. In *McCullum v. United States*, 58-2 U.S.T.C. (CCH) ¶ 9,957 (N.D. Okla. 1958), a married couple had elected to come under the 1939 Oklahoma elective community property law and subsequently acquired property as joint tenants. The 1945 Oklahoma statute establishing a mandatory system of community property provided that all married couples who had elected under the earlier law held their property as community property from the effective date of the election. Following the husband's death in 1948, one-half of the property was reported on the federal estate tax return as community property. The court held that the wife was entitled to the I.R.C. § 1014(b)(6) step-up in basis for her half of the property despite the joint tenancy form of the title, since that form of title did not prevent the property from being classified as community property under Oklahoma law.

Another decision bearing on this subject is *Estate of Chaddock v. Commissioner*, 54 T.C. 1667 (1970), in which the court held that, under Texas law, a husband and wife's taking title to certain community property stock as joint tenants with right of survivorship was ineffectual as a contract to create a joint tenancy out of their community property. Thus, when the husband died intestate, his community property interest in the stock immediately vested in his son as heir at law. Since the joint tenancy was not recognized, it follows that a full adjustment to the basis of both halves of the community property would be allowable under I.R.C. § 1014(b)(6), although that precise issue was not before the court.

Revenue Ruling 68-80, 1968-1 C.B. 348, held intent to be an issue when the reclassification occurred in the context of removing community property to a common law state. The ruling involved New Mexico community property that was converted into a Virginia tenancy in common. It appears that both interests in the property did not receive a full adjustment in basis at the death of the first cotenant, because the spouses intended to reclassify their community property as a common law tenancy. Absent that intent, it appears that the source or tracing principles discussed in chapter 13, *infra*, apply, and that the property does not lose its character as community property merely because a common law property form of holding title was adopted when the property was removed to a common law state. For federal tax purposes, it has been recognized that transportation of community property from a community property jurisdiction to a common law property jurisdiction does not cause the community property to lose its character. See *Johnson v. Commissioner*, 105 F.2d 454 (8th Cir. 1939); Rev. Rul. 63-169, 1963-2 C.B. 14, *obsoleted by* Rev. Rul. 80-325, 1980-2 C.B. 5; Field Serv. Advisory 19931609164 (ruling that Oregon residence held in joint tenancy that was purchased by couple with proceeds from sale of their California community property residence was community property for purposes of I.R.C. § 1014(b)(6), because under Oregon Uniform Disposition of Community Property Rights at Death Act, sales proceeds retained their character as community property).

Revenue Ruling 87-98, 1987-2 C.B. 206, permitted use of extrinsic evidence to determine the actual classification of property held by spouses in a common law joint tenancy with right of survivorship. The spouses affected by the ruling resided in an unidentified community property state. Under the law of the domiciliary state, spouses could hold property in joint tenancy with right of survivorship or in other common law estates. If title was taken to property in a common law form of ownership, a presumption was raised that the spouses intended to terminate any community property interest and transmute it into a separate property form of ownership. This presumption could be overcome by evidence that the spouses intended that the property not be transmuted into separate property. The law of the domiciliary state provided that an express statement of such intent in joint wills was effective to prevent a transmutation from occurring. The spouses' wills contained such a declaration at the time of the first spouse's death. Under these circumstances, the IRS ruled that when property held in a common law form of ownership is determined to be community property under applicable state law, it will be regarded as community property for

purposes of I.R.C. § 1014(b)(6) and will be allowed a full adjustment to basis.

A different result was reached in *Estate of Young*, 110 T.C. 297 (1998), in which the Tax Court held that California real estate held by a couple as joint tenants was joint tenancy property and not community property for purposes of I.R.C. § 1014(b)(6), notwithstanding a determination by the local California probate court that the property should be classified as community property. The couple acquired five parcels of real estate, in each case taking title as joint tenants with right of survivorship. In reviewing the case, the court began by stating that under California law joint tenancy and community property are mutually exclusive forms of property ownership and, while there is a strong presumption that property acquired during marriage is community property, there is a rebuttable presumption that the character of the property is as set forth in the deed. The court then noted that no evidence of either an oral or written transmutation of the real estate to community property was submitted in the probate court hearing, and therefore, the probate court's determination was not controlling. The court also found unpersuasive the testimony of the surviving spouse that a real estate broker recommended the joint tenancy to avoid probate and that she thought she owned one-half of the properties as her community property share. Noting that the surviving spouse did not speak, write, or understand English, the court found that there was no mutual agreement between the couple that the real estate was community property.

Based on the rulings and cases involving joint tenancies, it appears clear that regardless of the form in which title is taken, if the property would be treated as community property under state law, the IRS will follow that result and not attempt to apply a separate federal test to determine whether the property qualifies as community property for purposes of the full basis adjustment under I.R.C. § 1014(b)(6). Conversely, if taking title to property as joint tenants or tenants in common effectively transmutes the property's character from community to separate property under applicable state law, then the property will not be considered community property for purposes of I.R.C. § 1014(b)(6).

The Tax Court's decision in *Young* may well be unique to California, which does not permit any form of survivorship community property. By contrast, in Wisconsin, section 766.60(4) operates to virtually preclude the creation of common law joint tenancies and tenancies in common after the determination date in the absence of a marital property

agreement. Section 766.60(4)(b) specifically provides that if a document of title, instrument of transfer, or bill of sale expresses an intent to establish a joint tenancy exclusively between spouses after the determination date, the property is survivorship marital property; if it evidences an intent to establish a tenancy in common exclusively between spouses, the property is marital property. Because of this, the rules in *McCollum* and *Estate of Chaddock* (discussed above), that community property prevails over an attempt to hold property in a common law form of ownership, should apply to post-determination date joint tenancies exclusively between spouses, unless the tenancies were specifically created by marital property agreement.

On the other hand, the incidents of joint tenancy or tenancy in common will apply to marital property added to spousal joint tenancies or tenancies in common established before the determination date if there is a conflict. Wis. Stat. § 766.60(4)(a). The proper analysis appears to be that the addition or contribution of marital property to preexisting common law property will remain a marital property component, subject to the incidents of the joint tenancy or the tenancy in common only in the event of conflict. The Legislative Council Note to section 71.05(10)(e) (the Wisconsin basis-adjustment statute) supports the view that the marital property component of a joint tenancy does not lose its character as such for purposes of a full basis adjustment for Wisconsin income tax purposes. Tax Provisions of the Marital Property Implementation Law: Supplemental Explanatory Notes (1985 Wisconsin Acts 29 and 37), Wisconsin Legislative Council Staff Information Memorandum 85-7, Part II at 8. It should be noted, however, that the DOR, without citing any specific authority, takes the position that a marital property component in a joint tenancy or tenancy in common asset will not receive a full basis adjustment for Wisconsin income tax purposes. See DOR Pub'n 113, *supra* § 9.6, at 3.

### **b. Survivorship Marital Property Assets [§ 9.30]**

Closely related questions arise with respect to assets held as survivorship marital property, another optional form of holding property permitted by section 766.60(5). Again, the issue is whether the survivorship feature, a device intended primarily to avoid probate, will cause the survivorship marital property to be regarded as something other than community property for purposes of application of I.R.C. § 1014(b)(6).

The *Tax Practitioner Newsletter* (Apr. 1988) of the District Director of the IRS, Milwaukee District, stated the following: “Based upon advice received from the National Office, survivorship marital property will definitely be considered community property for federal income tax basis purposes. This means, upon the death of the first spouse, a full step up in basis will be received under I.R.C. section 1014.” *See also* DOR Publ’n 113, *supra* § 9.6, at 30.

Survivorship marital property is materially unlike joint tenancy with right of survivorship or common law tenancy by the entireties. This lack of similarity stems from the inability to unilaterally destroy the attributes of marital property, the preservation of creditors’ rights during the marriage in the same manner as other marital property, and the structuring of the survivorship marital property statute to clarify that it is marital property (with all the incidents of that classification) passing by a statutory nontestamentary disposition at death. Thus, for purposes of I.R.C. § 1014(b)(6), treating survivorship marital property in the same manner as marital property without the survivorship feature is clearly appropriate.

## **6. Basis Adjustment for Marital Property Partnerships [§ 9.31]**

If marital property assets are used in a family business that is treated by the spouses as a partnership for tax purposes, it may be necessary for the partnership to make elections under I.R.C. §§ 743 and 754 to obtain a full basis adjustment for the surviving spouse’s one-half interest in the marital property assets held by the partnership. This is because, in a two-member partnership, the Internal Revenue Code and Treasury regulations specifically provide that the partnership is not considered terminated upon the death of one partner if the estate or other successor in interest of the deceased partner “continues to share in the profits or losses of the partnership business.” Treas. Reg. § 1.708-1(b)(1)(i)(a); *see also* I.R.C. § 708(b)(1)(A).

The foregoing result will be extremely difficult to avoid if a husband and wife operate a business as a family partnership using assets that originally were marital property. Once the assets are contributed to the partnership, the marital property classification is transferred to the spouses’ respective partnership interests. As a result, the basis-election provisions of I.R.C. §§ 743 and 754 may be required to preserve basis

adjustment benefits inside the partnership regardless of whether the partnership is continued or wound up. Of course, the full adjustment to the basis of the partnership interests themselves is likely to ameliorate adverse capital-gains consequences when the partnership is finally liquidated and its assets are distributed to the surviving spouse and the deceased spouse's estate.

*Estate of Skaggs v. Commissioner*, 75 T.C. 191(1980), *aff'd*, 672 F.2d 756 (9th Cir. 1982), illustrates the potential problem if an effective election is not made under I.R.C. §§ 743 and 754. In *Estate of Skaggs*, a California husband and wife operated a ranch as partners under a written agreement. Their respective partnership interests were community property. The husband died on the last day of the calendar year. In the following year, his estate and the surviving spouse treated the partnership as terminated and assigned a stepped-up basis under I.R.C. § 1014(b)(6) to crops sold and depreciable assets for both halves of the farm operation. Because the partnership was viewed as terminated, no election was made under I.R.C. §§ 743 and 754 to make an internal adjustment in the basis of the partnership assets to match the external basis of the partnership interests owned by the estate and the surviving spouse.

Because the partnership did not terminate on the husband's date of death and because the estate and the surviving spouse continued to share the income from the ranching operation, the Tax Court held that an election under I.R.C. §§ 743 and 754 was necessary. Accordingly, the step-up in value of the partnership assets (as opposed to the partnership interests of the spouses) was denied, with major adverse tax consequences.

This problem can now be avoided by married couples operating a business as an LLC or partnership by electing to treat the business as a disregarded entity for tax purposes. *See supra* § 9.15. If such an election is made, the assets of the LLC or partnership will be deemed to be owned directly by the spouses and will qualify for a full basis adjustment under I.R.C. § 1014(b)(6).



## **7. Special Basis-adjustment Rule for Transfers of Appreciated Property Acquired Within One Year of Death [§ 9.32]**

A special rule under I.R.C. § 1014(e) denies a basis adjustment at death to certain transfers of appreciated property that were acquired by the decedent by gift during the one-year period preceding his or her death. The rule applies to transfers in which the appreciated property is retransferred to the original donor (or that person's spouse) by the decedent. The policy behind the rule is to prevent "gifts" of property to terminally ill persons that are then retransferred to the donor at death with a stepped-up basis.

This provision may have implications under the Act. For example, if spouses enter into a marital property agreement reclassifying the individual or predetermination date property assets of one spouse as marital property under circumstances in which there is no consideration for the reclassification, a "gift" of one-half of the former individual or predetermination date property assets may be considered to have been made to the other spouse. If the donee spouse then dies within one year of executing the agreement, leaving his or her one-half share of the newly classified marital property assets to the surviving donor spouse, will such share receive a basis adjustment under I.R.C. § 1014(b)?

The answer depends on whether a reclassification of individual or predetermination date property assets by marital property agreement (or otherwise) constitutes a transfer by gift within the meaning of I.R.C. § 1014(e). If the reclassification does constitute a gift, a basis adjustment will likely be denied to the deceased donee spouse's one-half interest if such interest is retransferred to the surviving donor spouse. On the other hand, if the deceased donee spouse transfers the marital property interest received by virtue of the agreement to a third person at death, the basis adjustment should be allowed. For example, if the deceased donee spouse transfers the marital property interest to a credit-shelter bypass trust in which the surviving donor spouse has only a discretionary interest, there is a strong argument that I.R.C. § 1014(e) does not apply because the surviving spouse has not directly received the transferred property back. It is less certain whether I.R.C. § 1014(e) will be avoided if the deceased donee spouse's marital property interest is transferred to a qualified terminable interest property (QTIP) marital trust in which the donor surviving spouse will have a mandatory income interest. Although

there is no authority on the issue, it appears that at least the portion of the QTIP trust allocable to the surviving donor spouse's lifetime income interest will be subject to I.R.C. § 1014(e) and will not receive a basis adjustment.

Revenue Ruling 77-359, 1977-2 C.B. 24, involving a Washington community property classification agreement, may support the view that transmutation of separate (i.e., individual or predetermination date) property into community (i.e., marital) property by a classification agreement constitutes a gift to the extent that there is inadequate consideration for the transfer. *See also* Priv. Ltr. Rul. 8929046 (July 21, 1989) (holding that agreement transmuting parties' community property into separate property and allocating it unequally between them constitutes gift to extent that value of separate property received by one spouse exceeds value of that received by the other).

DOR Publication 113 states that the IRS takes the position that the surviving donor spouse who reacquires his or her one-half share in former marital property assets from the deceased spouse within one year after execution of the marital property agreement is not entitled to a basis adjustment on the interest received from the decedent through application of I.R.C. § 1014(e). DOR Publ'n 113, *supra* § 9.6, at 31. DOR Publication 113 also states that the IRS takes the position that although a formal ruling has not been rendered, the denial of a basis adjustment to the decedent's one-half share of the former marital property assets would also appear to foreclose a similar adjustment under I.R.C. § 1014(b)(6) to the surviving donor spouse's retained one-half interest. *Id.*

It can be argued that the application of I.R.C. § 1014(e) cannot be avoided even by transferring assets under a marital property agreement in such a way that there is adequate consideration for the transfer. The applicability of I.R.C. § 1014(e) depends on the acquisition of appreciated property by the decedent "by gift" during the one-year period ending on the date of his or her death. Normally, transfers for adequate consideration are not gifts. However, I.R.C. § 1041(b) treats all transfers of property from one spouse to the other spouse as acquisitions by gift, without any exception for transfers for full or partial consideration. I.R.C. § 1041(b)(1); *see supra* § 9.7. The rule that any transfer of property from one spouse to the other spouse is treated as a gift is applied "for purposes of this subtitle." I.R.C. § 1041(b)(1). This refers to all

provisions of the Internal Revenue Code dealing with income taxes, including I.R.C. § 1014(e).

The denial of a basis adjustment under I.R.C. § 1014(e) should not apply to either (1) the reclassification as marital property of tenancy-in-common assets owned in equal shares by the spouses, or (2) the reclassification as survivorship marital property of joint-tenancy assets owned exclusively by the spouses, because the shares of ownership would remain unchanged and no gift would occur as a result of such reclassification.

It appears that I.R.C. § 1014(e) also does not apply if the donor spouse is the first to die. This is because the deceased donor spouse's one-half interest is includible in his or her gross estate directly under I.R.C. § 2033. Moreover, the decedent did not receive his or her one-half interest in the newly created marital property assets by gift during the one-year period preceding his or her death but retained it from the individual property assets that were the original subject of the gift. This will be true even if the deceased donor spouse's interest passes to the surviving donee spouse. The surviving donee spouse should be entitled to a full basis adjustment for his or her one-half interest in the newly created marital property assets received by way of the gift, since this interest is not one that is reacquired from a decedent by the original donor but is already owned by the donee spouse before the death of the donor spouse. In short, the death of the donor spouse in the foregoing example should not bring I.R.C. § 1014(e) into play at all. This result is appropriate, given that if the reclassification of the individual property to marital property had never occurred in the first place, the entire value of the property would have been included in the deceased spouse's estate and qualified for a full basis adjustment.

## **8. Basis Adjustment for Assets Held in Revocable Trusts [§ 9.33]**

The IRS has ruled that community property assets held in a trust that was fully revocable by either or both spouses during their joint lifetimes were entitled to a full basis adjustment under I.R.C. § 1014(b)(6). Rev. Rul. 66-283, 1966-2 C.B. 297.

Even if a Wisconsin revocable trust is funded after the determination date with marital property assets held by one spouse, and that spouse

retains the sole power to amend or revoke the trust, the benefits of the full basis adjustment should be available. This is because section 766.31(5) provides that the transfer of property to a trust does not by itself change the classification of the property. Accordingly, marital property assets transferred to a revocable trust should remain classified as marital property, and the full basis adjustment under I.R.C. § 1014(b)(6) should be available.

## **H. Federal Income Tax: Grantor Trust Issues Raised by Transfers of Marital Property [§ 9.34]**

The grantor trust rules of I.R.C. §§ 671 to 679 are familiar features in the tax planning landscape. These sections cause the income and, with some exceptions, the capital gains of a trust (or a portion of a trust) over which the grantor exercises or retains certain enumerated rights or powers to be taxed to the grantor of the trust, on the theory that the grantor has not given up significant dominion and control over the assets. Among the offensive rights or powers are a reversionary interest in the grantor that is worth more than five percent of the value of the trust assets to which it applies at the inception of the trust (I.R.C. § 673); retention by the grantor of the direct or indirect power to control the beneficial enjoyment of income or principal of the trust (I.R.C. § 674); retention by the grantor of the power to borrow from or deal with the trust assets on terms more favorable than those available in the marketplace (I.R.C. § 675); reservation by the grantor of the power to revoke the trust (I.R.C. § 676); and the right of the grantor or the grantor's spouse to receive income from a trust, to have trust income accumulated for future distribution to one or both of them, to have trust income used to pay the premiums on life insurance policies on one or both of their lives, or to have trust income used to satisfy the grantor's legal obligation of support (I.R.C. § 677). In a number of these provisions, exercise of the right or power is permissible if approval or consent is required from a person having a substantial beneficial interest in the trust that would be adversely affected by the exercise or nonexercise of the power. In addition, certain I.R.C. § 674 powers to control beneficial enjoyment will not be taxed to the grantor if exercised solely by an independent trustee. I.R.C. § 674(c).

The grantor-trust rules may apply in a number of situations in which marital property assets are intentionally or unintentionally transferred to a revocable or irrevocable trust. Some examples follow, in the same

numerical sequence as the applicable sections of the Internal Revenue Code:

➤ **Example 1.** Wife transfers assets that she believes to be individual property, but that in fact contain a significant marital property component, to an irrevocable trust for the benefit of her children by a prior marriage. She names the controller of the corporation owned and operated by her husband as the trustee, because he is financially experienced and she believes he will be an independent trustee under I.R.C. § 674(c). The trust contains broad powers to accumulate or distribute income and to invade principal for the benefit of the beneficiaries.

Under these facts, the husband is an unintended grantor of one-half the marital property component of the assets transferred to the trust. Because of the husband's ownership and control of the corporation of which the trustee is an employee, the trustee is not independent of the husband. I.R.C. § 674(c). Accordingly, the income and gains from the portion of the trust attributable to the husband's one-half marital property interest apparently are includible on the husband and wife's joint return by virtue of I.R.C. § 674.

➤ **Example 2.** Husband establishes an irrevocable trust for the benefit of his and his wife's children with property consisting of certain inherited stock in a closely held family business that he believes to be his individual property. The income of the trust is payable to the children, but during the wife's lifetime the trustee is authorized to invade principal for her benefit in the event of an emergency. Unknown to the husband and wife, a portion of the individual property assets is marital property as a result of substantial appreciation through the husband's substantial uncompensated efforts. The terms of the trust permit the family business corporation to repurchase the stock from the trust at a formula price that is substantially below market value, provided that the wife consents.

Because of the presence of a marital property interest in the assets of the trust, the wife may be an unintended grantor and thus unable to act as an adverse party for purposes of agreeing to the buyout of the closely held shares at a below-market formula price. The trust apparently will be treated as a grantor trust under I.R.C. § 675 and the

capital gains will be taxable to the husband and wife, rather than to the trust.

➤ **Example 3.** Wife creates an irrevocable trust funded with marital property assets over which she exercises exclusive management and control. The income of the trust is distributable to the husband and wife during their lifetimes. Following their deaths, the remainder interest passes to their children.

This trust will be a grantor trust under I.R.C. § 677 because of the right of the grantor and her husband to receive the income.

➤ **Example 4.** Husband, who has sole management and control of certain marital property assets, transfers the assets to a revocable trust. The trust provides for distribution of income to the husband and his wife during their joint lifetimes, and then to the survivor, with a remainder to the children upon the survivor's death. The trust grants the trustee powers to invade principal for the benefit of the beneficiaries, limited by an ascertainable standard. The husband alone retains the power to revoke the entire trust during his lifetime.

Because of the husband's retained power to revoke the entire trust, all its income and capital gains will be deemed taxable to him during his lifetime under I.R.C. § 676. If the husband dies before the wife, his power to revoke the trust is no longer exercisable. However, one-half of the trust is likely to be treated as a grantor trust as to the wife for as long as she has the right to recover her half of the marital property assets under section 766.70(6)(a). *See supra* §§ 9.18, .20. When that right of recovery expires, thus completing a gift of a remainder interest in the wife's one-half of the marital property to the children, the trust will no longer be considered a grantor trust as to the wife under I.R.C. § 676, but it may continue to be a grantor trust under the receipt-of-income rule of I.R.C. § 677.

These examples illustrate that a number of unexpected results can occur if marital property assets are used in the funding of trusts. An appreciation of these consequences is an important consideration in drafting trust documents. *See infra* ch. 10. The examples also underscore the desirability of clarifying the classification of assets by marital property agreement before their transfer into an irrevocable trust.

## I. Federal Income Tax: Effect of Marriage Agreements

### [§ 9.35]

Several revenue rulings have recognized that it is possible to reclassify property interests by agreement under state law. Revenue Ruling 77-359, 1977-2 C.B. 24, *obsolete in part* by Revenue Ruling 88-85, 1988-2 C.B. 333), specifically recognized that under Washington law a husband and wife may reclassify their presently owned or future acquired separate property as community property and indicated that such reclassification would be binding for income tax purposes. The ruling states as follows:

[W]here a husband and wife residing in the State of Washington agree in writing that all presently owned property and all property to be acquired thereafter, both real and personal, will be community property, such agreement changes the status of presently owned separate property and subsequently acquired separate property to community property.

In the same ruling, however, the IRS advised that to the extent an agreement purports to convert the income from separate property into community property without reclassifying the separate property itself into community property, the spouses will not be permitted to split that income for federal income tax purposes if they file separate income tax returns. This ruling seems sound because, as the ruling indicates, an attempt to convert the income from separate property to community property without a reclassification of the property that produces the income is an assignment of income.

In a revenue ruling involving the question of prospective reclassification of earned income by agreement from community property to the separate property of the earner, the IRS again recognized that because such a reclassification by agreement was valid under California law, it would be respected for federal income tax purposes. Rev. Rul. 73-390, 1973-2 C.B. 12. In a companion ruling, Rev. Rul. 73-391, 1973-2 C.B. 12, the IRS intimated that the same treatment would be accorded to income from an investment asset if a valid agreement existed as to the property law characterization of the investment. *See also Fleming v. Commissioner*, 47 T.C.M. (CCH) 1281 (1984) (holding that valid agreement between spouses under New Mexico law had effect of reclassifying the husband's community property income from personal services into his separate income for tax purposes). Note, however, that the IRS apparently will not allow more than 50% of marital property

income to be allocated to the nonearner spouse by marital property agreement. DOR Publ'n 113, *supra* § 9.6, at 15.

Revenue Ruling 87-13, 1987-1 C.B. 20, recognizes that under the Act, Wisconsin spouses may alter their property rights by marital property agreement and, by implication, change the tax treatment of their income, at least prospectively.

While the IRS recognizes that spouses may enter into a valid marital property agreement recharacterizing their earned or investment income as the individual income of the earning or recipient spouse, historically the IRS has resisted attempts to retroactively reclassify income (as distinguished from the property in which the income was invested) once it has been earned or received. In effect, all the events that fix the amount of income tax and determine the liability of the taxpayer to pay it must occur in advance of assessment and during the taxable year in question. See *United States v. Anderson*, 269 U.S. 422, 441(1926); see also *United States v. Mitchell*, 403 U.S. 190 (1971). In *Mitchell*, a wife who was separated from her husband was not permitted to avoid federal income tax obligations on her share of community income for years in which the community income had not been disclosed by the husband and no returns had been filed by either spouse. The wife had exercised her statutory option under the Louisiana Code to exonerate herself from debts contracted during marriage by renouncing her community property rights. The Court observed that this state law did not enable the wife to avoid her federal tax liability. These cases arguably preclude after-the-fact efforts by the spouses to attribute income from one to the other, or to allocate income as between themselves, to achieve perceived tax benefits.

The IRS does not prescribe any specific notification requirements with respect to a marital property agreement reclassifying income. The IRS will accept marital property agreements at the time of taxpayer contact for income-reporting purposes. DOR Publ'n 113, *supra* § 9.6, at 16. The IRS suggests that it is appropriate to furnish a copy of the marital property agreement to the IRS at the time it is executed. *Id.* Agreements should be mailed to the following address:

Internal Revenue Service  
SB/SE Advisory, Stop 5303 MIL  
211 W. Wisconsin Avenue  
Milwaukee, WI 53203



The Act itself might preclude a retroactive reclassification that adversely affects a tax liability owed to the IRS. Section 766.55(4m) states that no provision of a marital property agreement (or of a decree under section 766.70 for interspousal remedies) adversely affects the interest of a creditor unless the creditor had actual knowledge of that provision when the obligation was incurred. For purposes of section 766.55(4m), the term *creditor* broadly refers to any person to whom an obligation is owed. Thus, a retroactive attempt to reclassify income by marital property agreement that would adversely affect the interest of the IRS may be prohibited under section 766.55(4m). See section 9.52, *infra*, for a discussion of the effect of marital property agreements and unilateral statements for Wisconsin income tax purposes.

Some attorneys have attempted to use a marital property agreement or a divorce property settlement agreement to retroactively characterize the income or deductions of the spouses during the period before the entry of the judgment of dissolution. As indicated above, it is the position of the IRS that such an attempted retroactive reclassification of income by agreement will not be binding for federal income tax purposes. DOR Publ'n 113, *supra* § 9.6, at 15.

The courts have supported the position of the IRS that state court judgments that purport to retroactively recharacterize or reallocate items of income will not be determinative for federal tax purposes. See *Brent v. Commissioner*, 630 F.2d 356 (5th Cir. 1980) (holding that although divorce decree was given retroactive effect for state law purposes, it did not alter federal tax treatment of income earned in prior year); *Daine v. Commissioner*, 168 F.2d 449 (2d Cir. 1948) (not giving effect, for tax purposes, of retroactive judgment affecting treatment of alimony payments in prior year); *West v. Commissioner*, 131 F.2d 46 (9th Cir. 1942) (not recognizing, for tax purposes, retroactive dissolution of divorce decree and reinstatement of marital community).

Attempts to legislate retroactive application of divorce decrees to affect the income tax consequences for the spouses have been met with similar skepticism by the IRS. For example, Revenue Ruling 74-393, 1974-2 C.B. 28, examined the income tax effect of article 155 of the Louisiana Civil Code, which made the final judgment of divorce or separation retroactive to the date of filing of the original action. This was intended to permit each spouse to report the income he or she received during the pendency of the dissolution proceedings as if he or she were unmarried. The IRS concluded that under Louisiana law the

marital community continues in existence after the suit for divorce has been filed and up to the time the final judgment in the suit has been rendered, despite the statute giving retroactive effect to the judgment. Accordingly, if either spouse receives community income while the divorce is pending, each spouse has equal ownership rights in the income and corresponding federal income tax liability for his or her one-half share of it. Revenue Ruling 74-393 should apply with equal force in Wisconsin. *See* Rev. Rul. 87-13, 1987-1 C.B. 20.

Two approaches are available to avoid having to report income as part community property and part separate property in the year in which a divorce judgment is entered, and to avoid the related problem of ineffective retroactive income reclassification by agreement. First, the spouses may execute a marital property agreement during the pendency of the divorce to take effect at the beginning of what the parties anticipate will be their final tax year as spouses. Thus, each spouse may separately report only the income earned or received by him or her. Second, the spouses may arrange for the judgment of dissolution to be entered on December 31 of the year so that the entire year is subject to community income reporting. DOR Publ'n 113, *supra* § 9.6, at 17. Attorneys should avoid drafting agreements stating that “in the year a divorce judgment is entered” the income received by each spouse will be his or her respective individual property, since it is usually impossible to know with certainty what tax year will be affected until the judgment is entered. The tax authorities reviewing such agreements are likely to make the argument that such an agreement is retroactive. *See, e.g., id.* at 18. Under the terms of the agreement, the granting of the judgment of dissolution is the event that triggers a reclassification of income received during the portion of the year before the judgment is granted. If a future event is to trigger the reclassification of income, that event must occur *before* the income is generated. For example, a marital property agreement providing that all income received after the filing of a petition for divorce will be the individual income of the earning or recipient spouse is acceptable for Wisconsin purposes and should be acceptable for federal purposes, provided that the agreement is signed before the income is earned. *Id.*

Alternatively, it is not uncommon for divorce settlement agreements or judgments to include provisions assigning responsibility for the payment of federal income taxes. Often, these will provide that one spouse is responsible for any taxes owed for the last year in which a joint income tax return is filed. Joint returns may be filed during the pendency

of the divorce action, because the tax rates are more favorable than those available to married persons filing separate returns. Great care is required, however, because divorce property settlement agreements or judgments fixing responsibility for the payment of federal income taxes are not binding on the IRS. The tax liability on a joint return is joint and several. I.R.C. § 6013(d)(3). Therefore, the IRS may enforce collection of unpaid taxes against either party and leave it to the former spouses to resolve in state court the issue of compliance with the terms of the divorce settlement agreement or judgment. The most that can be achieved for divorcing spouses is either to ensure that the taxes shown on the return are paid when the return is filed or seek verification from the IRS that the taxes have been paid before the divorce judgment is rendered. See DOR Publ'n 113, *supra* § 9.6, at 19, for a description of the verification procedure.

The following sample provision is designed to assign responsibility for payment of taxes between divorcing spouses:

If either spouse is required to report and pay income tax on more income than he or she was legally entitled to receive during the calendar year in which the divorce judgment was entered (*excess income tax*), the spouse who was required to pay such excess income tax shall be reimbursed for the amount of the excess by the other spouse. By \_\_\_\_\_ [insert date] each spouse shall furnish the other spouse with a list of all income received by that spouse during 20\_\_ [insert year in which divorce judgment is expected to be entered] up to the date on which the divorce judgment is entered to enable such spouse to determine how much income should be reported.

## **J. Wisconsin Income Tax: Generally [§ 9.36]**

Wisconsin's income tax system may be described as being federalized in the sense that Wisconsin taxable income of natural persons and fiduciaries is derived from the definitions of federal taxable income and federal adjusted gross income in section 71.01(4). In the case of both natural persons and fiduciaries, Wisconsin taxable income is determined after making various modifications and transitional adjustments required by section 71.05.

The Wisconsin income tax statutes include a number of provisions that are designed to specifically address certain marital property issues. For example, the definition of Wisconsin taxable income in section 71.01(16) provides that losses, depreciation, recapture of benefits,

offsets, depletion, deductions, penalties, expenses, and other negative income items are to be determined according to the manner that income is or would be allocated for income tax purposes. Thus, the general rule under section 71.01(16) is that the negative characteristics of income are generally to follow the positive characteristics for tax purposes, whether the property is predetermination date, individual, or marital property.

Under the general proportionate-allocation rule of section 71.01(16), negative income allocations ordinarily would be split between the spouses in the same ratio as the income from the property is allocated. In the case of spouses filing separate returns, however, the application of this general formula could be inequitable with regard to net rent or other net returns from nonmarital property assets owned by one spouse. The general rule could result in a windfall for the nonowning spouse because he or she would receive one-half of the net income (income less negative income items), plus an additional share of the negative income items attributable to nonmarital property assets, which would thereby reduce the amount of income subject to taxation on the nonowning spouse's separate return. To address this concern, all of the negative income items arising from nonmarital property assets are expressly allocated under section 71.01(16) to the spouse owning the property, despite the fact that net rent or other net returns from nonmarital property assets are classified as marital property income under the Act and thus are deemed to be owned in equal shares (unless the spouse owning such nonmarital property has executed a unilateral statement classifying such income as individual property). The application of this provision is of course limited to married persons filing separate returns, because the problem does not exist if all the income and all the negative income items of both spouses are included on a joint return filed by the spouses.

Under section 71.01(8), the terms *married person* and *spouse* are defined as persons determined to be married under I.R.C. § 7703(a), unless the context requires otherwise. The statute also provides that for tax purposes a decree of divorce, annulment, or legal separation terminates the marriage and the application of the Act to the property of the spouses after the date of the decree, unless the decree provides otherwise.

Another provision of interest is section 71.10(6)(d), which has potential significance if one or both of the spouses are not domiciled in Wisconsin for the entire taxable year. This section provides that the tax liability and reporting obligations of both spouses during the period a

spouse is not domiciled in Wisconsin shall be determined without regard to chapter 766, except as otherwise provided. The intent of this provision is that common law property concepts of title ownership will be applied in allocating the income of the spouses between Wisconsin and another jurisdiction. This statute addresses the concern that if chapter 766 were to apply, a spouse domiciled in Wisconsin might be able to shift one-half of his or her earnings or investment income to a spouse who was domiciled elsewhere, at least until the other spouse established domicile in Wisconsin.

The interaction of the Act with Wisconsin's rules on the satisfaction of marital tax obligations is addressed in section 71.91(3). This provision provides that all tax obligations to the state of Wisconsin incurred by a spouse during marriage and after December 31, 1985, or after establishment of a marital domicile in Wisconsin, whichever is later, are incurred in the interest of the marriage or the family and may be satisfied only under sections 766.55(2)(b) and 859.18. If one spouse is relieved of liability under the innocent spouse rules of subsection 71.10(6)(a), (b), or (6m), the other spouse's tax obligation may be satisfied only under section 766.55(2)(d) as an obligation incurred during marriage that is not a support, family-purpose, or premarital obligation, or by set-off under the provisions of sections 71.55(1), .80(3) or (3m), or .61(1).

## **K. Wisconsin Income Tax: Joint Return Filing [§ 9.37]**

### **1. Joint Returns [§ 9.38]**

The Act not only permits spouses to file joint returns in Wisconsin but also affirmatively encourages them to file jointly through adoption of a more favorable rate structure. Subsections 71.03(2)(d) through (l) are based on I.R.C. § 6013 and adopt parallel requirements for the filing of joint returns by married persons, either originally or after separate returns have been filed by the spouses. Married persons must file either a joint return or a separate return. Married persons who qualify to file a joint federal return may file a Wisconsin joint return. It is unclear whether married persons who file separate federal returns also must file separately in Wisconsin, or whether they are permitted to file a Wisconsin joint return. Similar to the federal rule, a husband and wife may file a Wisconsin joint income tax return even though only one spouse has income or deductions. Wis. Stat. § 71.03(2)(d). There are

only a few exceptions to the broad availability of joint returns for Wisconsin married couples:

1. A joint return may not be filed if either spouse at any time during the taxable year is a nonresident alien, unless certain elections under the Internal Revenue Code are in effect. Wis. Stat. § 71.03(2)(d)2.
2. No joint return may be filed if the husband and wife have different taxable years, unless the difference in taxable years is attributable solely to the death of either or both spouses. However, a joint return may not be filed if the surviving spouse remarries before the close of his or her taxable year. Wis. Stat. § 71.03(2)(d)3.

A joint return may also be filed by the decedent's personal representative and the surviving spouse, or by the surviving spouse alone if no personal representative is appointed. If a personal representative is appointed after the filing of a joint return by a surviving spouse, the personal representative may disaffirm the joint return by filing, within one year after the last day prescribed by law for filing the return of the surviving spouse, a separate return for the taxable year of the decedent for which the joint return was filed. If the joint return is disaffirmed, the return filed by the surviving spouse is the survivor's separate return and the tax on that return shall be determined by excluding all items properly included in the return of the decedent spouse. Wis. Stat. § 71.03(2)(e).

Spouses may file a joint return after one or both have filed separate returns even though the time prescribed by law for timely filing the return for that taxable year has expired. Wis. Stat. § 71.03(2)(g). All payments, credits, refunds, or other repayments made or allowed with respect to the separate returns of each spouse for that taxable year are taken into account in determining the extent to which the tax based on the joint return has been paid. If a joint return is filed under this provision, any election (other than an irrevocable election to file a separate return) made by either spouse with respect to the treatment of any income, deduction, or credit on that spouse's separate return for that taxable year may not be changed on the joint return. *Id.* The election to file a joint return after one or both spouses have filed separate returns may also be made in the taxable year in which one or both spouses die. Wis. Stat. § 71.03(2)(h). The joint return may be filed by the decedent's personal representative and the surviving spouse, if any.

The election to file a joint return after one or both spouses have filed separate returns is subject to several limitations described in section 71.03(2)(i). The most significant of these are the following:

1. The amount of the tax shown on the joint return must be paid in full at or before the time the joint return is filed.
2. The joint return may not be filed later than four years from the last date prescribed by law for filing the return for the taxable year in question, determined without regard to any extension of time granted to either spouse.
3. The joint return may not be filed if a notice of adjustment has been mailed to either spouse and the spouse files a petition for redetermination, except that if both spouses request and the DOR consents, the election to file a joint return may be made; the joint return may not be filed if either spouse has commenced a suit for recovery of any part of the tax for that taxable year.
4. The joint return may not be filed if either spouse has entered into a closing agreement or a compromise of any civil or criminal case against the other spouse with respect to that taxable year.

Section 71.03(2)(m) permits spouses who have filed a joint return to change to separate returns if both spouses file on or before the last day for the timely filing of a return by either spouse. For a discussion of separate returns, see section 9.45, *infra*.

## **2. Rate Structure; Married Persons' Credit [§ 9.39]**

The rate schedules in section 71.06(2) indicate that the tax brackets for married persons filing joint returns are exactly twice as large as those of married persons filing separately. Thus, if the spouses have equal incomes, the sum of their Wisconsin income taxes on separate returns will exactly equal the tax due on a joint return. A disparity develops as the spouses' incomes grow more and more unequal, so that in single-earner families, filing separate returns ordinarily makes little sense because it produces a greater tax than a joint return. The tax brackets and rates for single individuals and fiduciaries in section 71.06(1) fall midway between those for married persons filing jointly and married persons filing separately.

To mitigate some of the adverse impact on married couples filing joint returns when both spouses have earned income, a married persons' credit was adopted. This credit is an amount equal to three percent of the earned income of the spouse with the lower income, but not exceeding \$480. Wis. Stat. § 71.07(6)(am)2.d. The computation of earned income is made "notwithstanding the fact that each spouse owns an undivided one-half interest in the whole of marital property." Wis. Stat. § 71.07(6)(am)1. A marital property agreement or a unilateral statement under chapter 766 transferring income between the spouses has no effect in computing earned income for purposes of this credit. The earned income credit may not exceed the amount of Wisconsin net income taxes otherwise due on the joint return. Amounts received by one spouse in the employ of the other spouse may be used to compute the married persons' credit.

For purposes of the married persons' credit, earned income includes only earned income allocable to Wisconsin. The married persons' credit is not available to married persons who reduce their gross income by foreign earned income under I.R.C. § 911 or by income earned in certain specified United States possessions under I.R.C. § 931. Earned income is linked to the definition of *qualified earned income* in I.R.C. § 221(b), plus certain employee business expenses under I.R.C. § 62(2)(B), (C), and (D) (provided such income or expenses are allocable to Wisconsin), minus the amount of excludable disability income and any other amount of earned income not subject to Wisconsin income tax.

### **3. Joint and Several Liability [§ 9.40]**

Married persons filing a joint return are jointly and severally liable for the tax, interest, penalties, fees, additions to tax, and additional assessments applicable to the return. Wis. Stat. § 71.10(6)(a). An innocent spouse is relieved of liability for a joint return in the same manner as specified in I.R.C. § 6015, notwithstanding the amount or percentage of the understatement. *Id.* See section 9.3, *supra*, for a discussion of the federal innocent-spouse provisions, and section 9.46, *infra*, for a discussion of the Wisconsin version.

As demonstrated by *Smith v. Wisconsin Department of Revenue*, No. 93 CV 356, [1993–1998 Transfer Binder], St. Tax. Rep. (CCH) ¶ 400-098 (Wis. Cir. Ct. Barron County Apr. 7, 1994), the imposition of joint and several liability can lead to a harsh result when only one spouse



receives the benefit of the taxable income. In *Smith*, an ex-husband was found jointly and severally liable for Wisconsin income taxes owed on capital gains realized from the sale of a residence that he owned with his ex-wife because they filed a joint return for the taxable year at issue, even though the proceeds from the sale were awarded to the ex-wife in the divorce decree. The court ruled that the fact that the ex-wife received all the proceeds from the sale was irrelevant for purposes of imposing joint and several liability on the ex-husband under section 71.10(6)(a).

#### **4. Refunds and Overpayments; Satisfaction of Certain Obligations [§ 9.41]**

Both spouses must sign claims for refund or credit of overpayments with respect to joint returns. Wis. Stat. § 71.75(6). A marital property agreement or unilateral statement cannot affect the requirements for claims for refund or credit under this provision. Under section 71.75(8), a refund payable on the basis of a joint return must be issued jointly to the persons who filed the return. However, if a judgment of divorce apportions any refund that may be due to the formerly married couple to one of the former spouses, or between the spouses, and if they include with their income tax return a copy of that portion of the divorce judgment that relates to the apportionment of their tax refund, the DOR will issue the refund check to the person to whom the refund is awarded under the divorce judgment or will issue separate checks to each of the former spouses according to the apportionment terms of the divorce judgment. Wis. Stat. § 71.75(8).

The rules for the crediting of overpayments, homestead and farmland preservation credits, and other refunds, including any interest allowed, resulting from joint returns are set forth in section 71.80(3m). As a general rule, the DOR may credit any overpayment, credit, or refund on a joint return against any liability of either spouse or both spouses for taxes, debts to the state under section 71.93, or delinquent child support obligations under section 49.855 that were incurred during marriage and after December 31, 1985, or after both spouses are domiciled in Wisconsin, whichever is later. This authorization is made subject to the innocent-spouse provisions in subsections 71.10(6)(a), (b), and (6m). Wis. Stat. § 71.80(3m)(a); *see also* Wis. Stat. § 71.10(6m).

Proportionate crediting of overpayments, credits, or refunds from a joint return is also authorized if the spouse incurred the liability to the

DOR either before January 1, 1986, or before marriage, whichever is later. This applies to debts to the state or certain delinquent child support obligations that are not deemed to be incurred in the interest of the marriage or the family and also to amounts that are subject to the innocent-spouse or former-spouse reallocation rules in subsections 71.10(6)(a), (b), and (6m). Wis. Stat. § 71.80(3m)(b). Only the proportion that the Wisconsin adjusted gross income that would have been the spouse's property but for the marriage bears to both spouses' total adjusted gross income can be offset. *Id.* These provisions effectively create debt-satisfaction rules similar to those found in subsections 766.55(2)(b) and (c) and eliminate the necessity for the DOR to credit the overpayments, credits, and refunds in accordance with the marshalling provisions of section 766.55(2)(d). *See supra* § 9.36 (discussion of satisfaction of tax obligations under section 71.91(3)).

The offset provisions in section 71.80(3m) require the DOR to provide notice to the spouses of its intent to use the crediting process. Wis. Stat. § 71.80(3m)(c). Within 20 days after the date of the notice, the nonobligated spouse is allowed to prove by clear and convincing evidence that the overpayment, credit, or refund is his or her nonmarital property. Wis. Stat. § 71.80(3m)(intro.). If a spouse does not receive the requisite notice, and if the DOR incorrectly credits the overpayment, refund, or credit, a claim for refund may be filed within two years after the date of the offset that was the subject of the notice. Wis. Stat. § 71.80(3m)(d).

It is not clear what effect a marital property agreement may have on the DOR's debt-satisfaction powers under section 71.80(3m) if the agreement is filed with the DOR before assessment of the liability. It is arguable that the marital property agreement should control, in the absence of a specific statutory provision to the contrary. On the other hand, it can also be argued that because section 71.75(6) limits the ability of a marital property agreement to affect the ownership of a refund or overpayment, that section similarly limits the ability of an agreement to vary the DOR's power to apply a refund or overpayment against the liability of either or both spouses under section 71.80(3m).

The DOR may not apply a refund otherwise due an individual against any tax liability owed to the DOR by the individual or by a former spouse of the individual if (1) a judgment of divorce apportions that liability to the former spouse, and (2) the individual includes with his or

her tax return a copy of the divorce judgment. *See* DOR Publ'n 109, *supra* § 9.6, at 16.

## **5. Joint Estimated Tax Payments [§ 9.42]**

Spouses may jointly pay estimated taxes unless they have different taxable years or unless one spouse is a nonresident alien. Wis. Stat. § 71.09(16). If the couple pays jointly, the provisions of section 71.09 otherwise applicable to individuals become applicable to the couple jointly. If a married person files a separate return for a taxable year for which a joint payment was made, the payments may be allocated between the spouses as they choose. If they do not agree on an allocation, the DOR will allocate the payments in proportion to the taxes shown on their separate returns. Thus, as a matter of administrative convenience, either the spouses or the DOR may allocate estimated tax payments regardless of whether the payments are made with marital property or individual property funds.

Section 71.09(13) adopts the federal system for determining the amount of estimated tax required to be paid to avoid the penalty for underpayment of estimated tax. Basically, the amount required to be paid by each installment due date is 25% of the lower of (1) 90% of the tax due for the taxable year, or (2) the tax due for the preceding year.

## **6. Miscellaneous Procedural Provisions [§ 9.43]**

The Wisconsin income tax law includes a number of procedural provisions that are designed to assist in the administration of the joint return filing provisions. For example, under section 71.74(11), if married persons have filed a joint return, a notice of additional assessment may be a joint notice, and a notice served on one spouse is proper notice to both spouses. If the spouses have different addresses when the notice of additional assessment is served, and if either spouse notifies the DOR in writing of those addresses, the DOR is required to serve a duplicate of the original notice on the spouse who has the address other than the address to which the original notice was sent, as long as no request for a redetermination or a petition for review has been commenced or finalized. Redetermination and appeal rights for the spouse who did not receive the original notice begin upon the service of a duplicate notice. *Id.* Under sections 71.74(8) and 71.88(1)(b), notices

to spouses regarding the determination or redetermination of a claim under the homestead credit, married persons' credit, and farmland preservation credit statutes must conform to the notice requirements of section 71.74(11).

With respect to petitions to the DOR for redetermination of an assessment, or appeals to the Wisconsin Tax Appeals Commission, the definitions of *person feeling aggrieved* and *person aggrieved* are found in section 71.87. They include the spouse of a person against whom an additional assessment was made or who was denied a claim for refund for a taxable year for which a separate return was filed. They also include either spouse for a taxable year for which a joint return was filed or could have been filed. This is appropriate, considering the family-purpose nature of Wisconsin income tax obligations under section 71.91(3). Under section 71.88(1)(a), a petition or appeal by one spouse is a petition or appeal by both. The requisite notification to the spouses that they may forestall the accrual of additional interest by depositing the amount of an additional assessment will be made jointly to the spouses, unless different addresses for the spouses are furnished to the DOR in writing. Wis. Stat. § 71.90(1).

In situations in which taxpayers report less than 75% of the net income properly assessable, the six-year statute of limitation in section 71.77(7) applies, rather than the normal four-year statute. The minimum threshold for making an assessment on a joint return under the extended period is \$200 of taxable income.

The confidentiality rules in section 71.78(4)(k) provide that a spouse or former spouse of a taxpayer may request and receive information from a return (or a claim for credit) filed by the taxpayer. This exception applies in only the following two circumstances: (1) the spouse or former spouse making the request may be liable for, or his or her property is subject to, a collection action with respect to a delinquency relating to the return or claim for credit; or (2) the DOR has issued an assessment or denial of claim to the spouse or former spouse with respect to the return or claim. Such disclosure is appropriate because tax obligations are classified as family-purpose obligations. Therefore, the marital property of a spouse or former spouse may be subject to satisfaction of the tax liability or the liability for the tax obligation of the other spouse may be assigned by court decree under chapter 766 or 767. Under section 71.78(4m), the DOR is permitted to disclose to the spouse or former spouse of a person who has filed a return or claim for credit

whether an extension for filing the return or claim was obtained, the extended due date, and the date on which the return or claim was actually filed with the DOR.

The Wisconsin income tax law also includes several procedural provisions designed to permit the DOR to make assessments in the alternative against married persons. Properly allocating income and assessing taxes are particular problems when the spouses are separated and filing separate returns in the year when the spouses are divorced. *See supra* §§ 9.5, .6. If the DOR is compelled to proceed against spouses sequentially, by the time the facts and law applicable to assessment of one spouse have been determined, the expiration of the statute of limitation may bar assessment of tax on income properly allocable to the other spouse. The innocent-spouse provision for married persons filing separate returns in section 71.10(6)(b) adds another complicating factor. *See infra* § 9.46. Accordingly, section 71.74(9) provides that if the DOR determines that liability for Wisconsin income tax exists and that more than one person may be liable, the DOR may assess the entire amount to each person, specifying that it is assessing in the alternative. Similarly, section 73.01(4)(i) permits the hearing of appeals from assessments in the alternative on a combined docket basis.

## **L. Wisconsin Income Tax: Separate Return Filing by Married Persons [§ 9.44]**

### **1. Separate Returns [§ 9.45]**

Although the filing of a joint return will generally provide significant tax benefits to a married couple, they are free to file separate Wisconsin income tax returns. For married persons filing separately, the Wisconsin treatment of deductible expenses allowed in the computation of the itemized deductions credit under section 71.07(5) is the same as the federal treatment of these deductions. DOR Publ'n 113, *supra* § 9.6, at 19. See section 9.6, *supra*, for a discussion of the federal treatment. Generally, expenses incurred to earn or produce marital property income are divided equally between the spouses. *Id.* Expenses incurred to earn or produce individual property income are allocated to the spouse who generates or receives the income, provided that spouse paid the expenses from his or her individual property. *Id.* at 20. Expenses that are not attributable to any specific category of income, such as medical expenses

or charitable contributions, are deductible by the spouse who pays them. If these personal deductions are paid from marital property funds, however, then the amounts are divided equally between the spouses. *Id.*

If married persons file separate returns for a taxable year for which a joint estimated tax payment was made, the estimated tax payment may be allocated between the spouses as they choose, but if they do not agree on an allocation, the DOR will allocate payment to each spouse on the basis of the ratio of taxes shown on their separate returns or pursuant to default assessment under section 71.74(3). Wis. Stat. § 71.09(16). If either spouse makes an estimated tax payment separately, no part of the payment may be allocated to the other spouse. *Id.* These allocation rules are adopted for administrative convenience and without regard to whether the estimated tax payments were made with marital property or individual property funds.

Unlike federal law, section 71.03(2)(m)1. provides that if the spouses have filed a joint return for a taxable year, they may file separate returns if they do so on or before the last day prescribed by law for timely filing of the return of either spouse. If a husband and wife change from a joint return to separate returns within the prescribed time, the tax paid on the joint return is allocated between them in proportion to the tax liability shown on each separate return. Wis. Stat. § 71.03(2)(m)2. A separate return may not be filed under this section unless the amount of tax shown on that separate return is paid in full on or before the date when the separate return is filed. Wis. Stat. § 71.03(2)(m)5.

In the taxable year in which one or both spouses die, either the surviving spouse or the decedent's personal representative may file a separate return after a joint return has been filed either by the surviving spouse or by the personal representative and the surviving spouse. Wis. Stat. § 71.03(2)(m)3. The time allowed the personal representative to disaffirm the previously filed joint return by filing a separate return does not establish a new due date for the return of the deceased spouse. Wis. Stat. § 71.03(2)(m)4.

The special provisions of I.R.C. § 66(a), which under certain circumstances allow separated spouses to report without regard to state community property laws the income earned by each, do not apply for Wisconsin income tax reporting purposes (the requirements of I.R.C. § 66(a) are discussed in section 9.5, *supra*). Wis. Stat. § 71.05(10)(f); DOR Publ'n 113, *supra* § 9.6, at 10. Consequently, while spouses who

are living apart may file separate federal returns reporting their income without regard to most of the Act's ownership principles (assuming that they meet the criteria established under I.R.C. § 66(a)), they cannot report their income in this fashion when filing their Wisconsin separate returns. For Wisconsin income tax reporting purposes, the spouses must report their respective shares of income on the basis of the marital property ownership principles established under the Act unless the specific relief provisions for innocent spouses filing separate returns apply. *See* Wis. Stat. § 71.10(6)(b) (discussed in section 9.46, *infra*).

Under section 71.64(1)(c), withholding taxes collected from “marital income” are to be allocated between the spouses in the same manner that the income is allocated or would be allocated. The term *marital income* is not defined, and thus it is not known whether it refers only to income classified as marital property under section 766.31(4). This provision apparently is in response to the concern that one-half of the earned income of an employee spouse may be allocated to a divorcing nonemployed spouse through application of section 766.31(4) and corresponding rules of taxation, while the employee spouse could claim all the withholding as a credit against his or her tax on the other half of the income. This would leave the nonemployed spouse with a tax liability and no share of the withholding taxes to credit against it. Meanwhile, the employee spouse might actually receive a refund by virtue of having all the withholding credited to him or her. *See* section 9.4, *supra*, for further discussion of the federal rules applicable to filing of separate returns by married persons.

The DOR's views on the subject of the filing of separate returns by spouses and former spouses is set forth in DOR Publ'n 109, *supra* § 9.6. The DOR suggests that spouses filing separate returns should each attach a copy of the worksheet included in the back of DOR Publication 109 to show how each computed the income, deductions, and credits he or she is reporting. *See also* DOR Publ'n 113, *supra* § 9.6, at 5.

## **2. Liability; Innocent-spouse Provisions [§ 9.46]**

Wisconsin does not follow the special federal tax rule found in I.R.C. § 66(a) for spouses “living apart all year.” Although the DOR proposed that a similar Wisconsin rule be adopted, the Legislature's Special Committee on Marital Property Implementation rejected this approach because the Act applies to spouses until dissolution of the marriage. *See*

DOR Publ'n 113, *supra* § 9.6, at 13. Instead, a much broader innocent-spouse statute, section 71.10(6)(b), which is based on the federal rules contained in I.R.C. § 66(b) and (c), was adopted in Wisconsin for spouses filing separately. See section 9.3, *supra*, for a discussion of the federal innocent-spouse provisions.

With respect to unreported marital property income, section 71.10(6)(b) provides that the DOR may not apply chapter 766 in assessing a taxpayer if the taxpayer failed to notify his or her spouse about the amount and nature of the income before the due date (including extensions) for filing a return for the taxable year in which the income was derived. Under such circumstances, the marital property income cannot be divided equally between the spouses. Instead, the DOR must include all the marital property income in the gross income of the taxpayer who failed to disclose and must exclude all of that income from the gross income of the taxpayer's spouse. The taxpayer's spouse who files a separate return under these circumstances may be relieved of liability for the tax, interest, and penalties with regard to the unreported marital property income in the manner specified in I.R.C. § 66(c). In addition, subsections 71.05(10)(f), (g), and (h) require appropriate adjustments to the federal adjusted gross income of a spouse filing separately to reflect the inapplicability of I.R.C. § 66(a), the applicability of the Wisconsin innocent-spouse provisions contained in section 71.10(6)(b)–(d), and any other differences between the treatment of marital property income for federal and Wisconsin income tax purposes. DOR Publ'n 113, *supra* § 9.6, at 12.

Under section 71.10(6)(b), the burden is placed on the spouse receiving the income to notify the nonrecipient spouse about the amount and nature of marital property income. *Id.* If the nonrecipient spouse is not notified by the due date, including extensions, for filing the recipient spouse's tax return, the nonrecipient is an innocent spouse with respect to that marital property income. *Id.* In the case of divorce, if the innocent-spouse rule applies, the DOR may assess only the recipient spouse, even if the couple's divorce decree provides that each spouse is liable for one-half of the couple's total tax liabilities. *Davis v. Wisconsin Dep't of Revenue*, [1998–2000 Transfer Binder], St. Tax. Rep. (CCH) ¶ 400–422 (Wis. Tax App. Comm'n 1999).

It appears that these requirements will be strictly construed. In *Bennett v. Wisconsin Department of Revenue*, [1986–1990 Transfer Binder] St. Tax Rep. (CCH) ¶ 203–105 (Wis. Tax App. Comm'n 1989),



both spouses had filed for and received extensions to file their 1986 federal returns, first to August 15, 1987, and then to October 15, 1987. The wife notified the husband of her 1986 earnings, withholding, and deductions by certified letter in July 1987. In September 1987, she filed her 1986 Wisconsin income tax return, reporting all her wages, interest income, and itemized deductions and none of her husband's income or deductions. On October 13, 1987, she was personally served with information concerning her husband's 1986 earnings, investment income and losses, and itemized deductions. Subsequently, the DOR assessed the wife for additional income taxes and interest under the provisions of section 71.74(9) (formerly section 71.11(21)(f)), which permits assessments in the alternative. The wife petitioned for reconsideration, raising the question whether the husband's notification regarding his marital property income two days before the extended due date for filing returns was timely and proper under section 71.10(6)(b) (formerly section 71.11(2m)). The Wisconsin Tax Appeals Commission concluded that the due date for filing the return is also the statutory due date by which one spouse is obligated to notify the other. Accordingly, the notifications by both the wife and the husband were timely, even though the husband's notification was received after the wife had filed her return. Consequently, both spouses were required to report one-half of their combined marital property income. Based on the commission's decision, it appears that a spouse's practical difficulty in using the proffered information to file a timely return is not sufficient to obtain innocent-spouse status.

Section 71.10(6)(b) does not specifically require the recipient spouse to notify the nonrecipient spouse for income tax purposes. If the recipient spouse does not provide notification about the nature and amount of marital property income over which he or she had control, the penalty is that the recipient spouse must report all of that marital property income as his or her own income. DOR Publ'n 113, *supra* § 9.6, at 13. Thus, failure to notify results in treatment similar to that provided in the federal "living apart all year" rule of I.R.C. § 66(a). *Id.* By not notifying, each spouse would be an innocent spouse with respect to the other's marital property income. *Id.*

In addition, the statute does not specify what constitutes adequate notification. *Id.* However, the DOR suggests that notification by certified mail, return receipt requested, should be adequate for purposes of the statute. *Id.* at 12. The DOR also indicates that a notice containing only a total dollar amount of income will probably be inadequate, since

the nonrecipient spouse will not know how to report it. *Id.* Further, if the recipient spouse fails to notify the nonrecipient about expenses, deductions, and withholdings relating to marital property income, the DOR may conclude that no notification took place and that the recipient spouse must report all the marital property income. *Id.* This stems from the requirement of section 71.01(16) that certain negative income items be allocated in the same manner as the income to which they relate (*see supra* § 9.36) and also from the similar rule in section 71.64(1)(c) pertaining to withholding (*see supra* § 9.45). DOR Publ'n 113, *supra* § 9.6, at 12.

A question may arise as to whether the disclosure of income in divorce proceedings constitutes adequate notification for purposes of the Wisconsin innocent-spouse statute. *Id.* at 18. In the absence of court decisions, the DOR has declined to provide any guidance and has suggested that the best solution is for the spouses to agree whether or not they will notify each other of the amount and nature of their marital property income. *Id.*

Whenever it is apparent to the DOR that there is a dispute between the spouses as to whether proper notification has occurred, it will issue assessments to both spouses in the alternative. *Id.* at 14. These assessments may reflect more than the total income of both spouses. *Id.* For example, if the recipient spouse reports one-half of the marital property income from his or her earnings or investments and the nonrecipient spouse fails to report the other half, the recipient spouse will be assessed tax on 100% of the marital property income he or she received (in effect denying that proper notification occurred). The nonrecipient will be assessed tax on one-half of the recipient's marital property income (in effect denying that spouse's claim to be an innocent spouse). *Id.* Upon final determination of the proper allocation and reporting of income, the DOR will adjust either or both spouses' incomes, expenses, and deductions, as appropriate. *Id.*

Under section 71.10(6m), innocent-spouse protection may also be applied to former spouses, whether or not they are remarried, who are filing a return for a period covering the former marriage. The rules for satisfaction of marital tax obligations under section 71.91(3) treat the liability of the noninnocent spouse as a nonfamily-purpose obligation. *See supra* § 9.36.

A chart comparing the differences between federal and Wisconsin innocent-spouse treatment is set forth in DOR Publ'n 113, *supra* § 9.6, at 14.

### **3. Refunds and Overpayments [§ 9.47]**

Section 71.75(8) specifically states that a refund payable on the basis of a separate return must be issued to the person who filed the return. Under section 71.75(6), a claim for refund or credit must be signed by the spouse who filed the separate return. Thus, it is not possible for married persons filing separate returns to credit all or part of the overpayment of one spouse against the tax liability of the other.

Section 71.80(3) authorizes the DOR to presume that any overpayment, homestead or farmland preservation credit, or refund on an individual or separate return is the nonmarital property of the filer, all of which may be credited against any tax liability, debt to the state under section 71.93, or delinquent child-support obligation under section 49.855 incurred by the filer before, during, or after a marriage. The filer's spouse or former spouse may file a claim for refund of amounts so credited if the spouse or former spouse can prove by clear and convincing evidence that all or part of the overpayment, credit, or refund was nonmarital property of the nonobligated spouse. Such a claim for refund must be filed within two years after the crediting by the DOR.

### **4. Separate Estimated Tax Payments [§ 9.48]**

At least by implication, section 71.09(16) makes clear that a married person may make separate estimated tax payments. The final sentence of this subsection states that if either spouse pays estimated tax separately, no part of the payment may be allocated to the other spouse.

## **M. Wisconsin Income Tax: Gain or Loss Transactions Between Spouses [§ 9.49]**

Wisconsin's income tax system has been federalized, in the sense that the taxable income of individuals is derived under section 71.01(4) from the definitions of federal taxable income and federal adjusted gross income. Accordingly, all of the nonrecognition rules encompassed in

I.R.C. § 1041 apply for purposes of determining the Wisconsin income tax treatment of transactions between spouses. *See supra* § 9.7.

## **N. Wisconsin Income Tax: Basis-adjustment Rules for Marital Property Assets [§ 9.50]**

The Wisconsin equivalent of I.R.C. § 1014(b)(6) (*see supra* § 9.24) is found in section 71.05(10)(e). The Wisconsin provision relates generally to modifications of Wisconsin adjusted gross income for adjustments to basis when the value of property acquired from a decedent is different for federal estate tax purposes and Wisconsin estate tax purposes.

➤ **Comment.** For a brief discussion of the current uncertainty regarding estate tax law, see the “Note to Readers” accompanying chapter 10, *infra*.

With respect to deaths of Wisconsin married persons occurring after 1991, the federal and the Wisconsin basis of assets acquired from a decedent normally will be identical because the Wisconsin inheritance tax was replaced, effective January 1, 1992, with a “pick-up” estate tax based on the federal estate tax credit for state death taxes. Wis. Stat. § 72.02. *But see* Wis. Stat. § 71.02(11m) (decoupling Wisconsin’s estate tax from the federal estate tax effective until December 31, 2007, and allowing the federal estate tax credit for state death taxes to be computed for Wisconsin estate tax purposes under the federal estate tax law in effect on December 31, 2000). Because differences between the federal and the Wisconsin basis were possible under the former Wisconsin inheritance tax law, sections 72.01–.35 (1985–86), the modification adjustments in section 71.05(10)(e) will continue to be relevant with respect to dispositions of property acquired from a decedent before 1992. Such modification adjustments could also become more relevant in the future if Wisconsin chooses to reinstate to maintain the independent estate tax system it maintained from 2002 through 2007. For a comprehensive discussion of the Wisconsin estate tax that was in effect for the tax years 2002–07, see Michael W. Wilcox, *Wisconsin’s New Estate Tax*, Wis. Law., Dec. 2001, at 10.

Under section 71.05(10)(e), if at the time of death at least 50% of the marital property assets held by the decedent and the decedent’s surviving spouse are includible for purposes of computing the federal estate tax on

the decedent's estate, all the decedent's assets (of whatever classification) and all of the surviving spouse's marital property assets are treated as property includible for Wisconsin death tax purposes and receive a basis adjustment. Section 71.05(10)(e) makes clear that while Wisconsin death tax values control in making basis determinations, property that passed to a spouse (and thus was exempt from inheritance tax under section 72.15(5) (1985–86)) will be deemed includible for Wisconsin death tax purposes, but property subject to the former joint-tenancy exclusion under section 72.12(6)(b) (1985–86) will not be deemed includible.

Although the issue is not free from doubt, the legislature appeared to have recognized that assets owned in joint tenancy may have a marital property component and, if so, both halves of that component are entitled to a basis adjustment. Specifically, the 1985 Trailer Bill Supplemental Tax Note to section 71.05(1)(g) (1985–86) states: “Each half of the marital property component of a property owned exclusively by the spouses in joint tenancy receives a basis adjusted to the date-of-death value. Otherwise, only the decedent's share of the nonmarital property component of such a joint tenancy receives an adjusted basis.”

This note indicates that a marital property component may be created in a predetermination date asset owned in joint tenancy, despite the prevalence of the “incidents” of the joint tenancy under section 766.60(4)(a) in the event of a conflict. *See supra* §§ 2.253–.255. The result is that both parts of the marital property component, along with one-half of the joint-tenancy component, would receive a Wisconsin income tax basis adjustment at the death of one of the spouses.

The foregoing analysis may not agree with the position of the IRS or the DOR on the appropriate methodology for calculating the basis adjustment for marital property assets at the death of a spouse. *See* DOR Publ'n 113, *supra* § 9.6, at 30. However, assuming that the nonmarital property component of a predetermination date asset titled in joint tenancy can be traced, the normal mixing-reclassification rule of section 766.63(1) will be avoided, and no policy reason exists why the marital property component of the asset titled in joint tenancy should not be recognized and receive a full basis adjustment for both federal and Wisconsin income tax purposes.

## **O. Wisconsin Income Tax: Modifications and Transitional Adjustments [§ 9.51]**

Among the modifications employed in arriving at Wisconsin taxable income that are relevant from a marital property perspective are those found in subsections 71.05(10)(f), (g), and (h). These include a modification to reflect the inapplicability of I.R.C. § 66(a) (federal innocent-spouse provision on income of spouses “living separate and apart,” *see supra* § 9.5); a modification to account for the different treatment of marital property agreements under section 71.10(6)(c); a modification to account for the different treatment that results under section 71.10(6)(d) when both spouses are not domiciled in Wisconsin for the entire taxable year; and a modification to account for the more liberal Wisconsin treatment of the separately filing innocent spouse under section 71.10(6)(b). Section 71.05(10)(h) also permits any other modifications (including those adopted by administrative rule) that are necessary to reflect any other differences between the treatment of marital income for federal income tax purposes and the treatment of such income under the Wisconsin income tax laws.

Another specific marital property related modification deals with treatment of excludable disability payments. Section 71.05(6)(b)4. makes it clear that if the spouses file a joint return and only one spouse is disabled, the maximum exclusion is either \$100 per week for each week that payments are received or the amount of the disability pay reported as income, whichever is less. This provision is designed to prevent both spouses from claiming the exclusion on the ground that the disability pay is a marital property asset. Moreover, only the disabled spouse who is divorced during a given taxable year may claim the exclusion. *Id.*

Section 71.05(6)(a)16. treats the court-approved exchange of former marital property interests between a surviving spouse and a distributee of the decedent spouse under section 857.03(2) as a nontaxable exchange for Wisconsin income tax purposes. Any loss recognized on such an exchange for federal income tax purposes is treated as a modification addition, *see* Wis. Stat. § 71.05(6)(a)16., and any gain recognized for federal income tax purposes in such an exchange is treated as a subtraction modification. Wis. Stat. § 71.05(6)(b)12. For basis-determination purposes, the exchange is treated as if each asset received in the exchange were acquired as a gift from the other party. Wis. Stat.

§ 71.05(12)(d); *see infra* § 12.178 (discussion of statutory requirements for court-approved property exchanges under section 766.31(3)(b)3.).

The modification provisions addressing an exchange between a surviving spouse and a distributee of the decedent spouse are apparently intended to avoid any uncertainties regarding the proper treatment of non-pro rata distributions of former marital property assets for federal income tax purposes. See section 9.20, *supra*, for a discussion of the federal income tax rules on this subject. If federal income tax law regarding non-pro rata distributions of former marital property assets between the surviving spouse and other distributees of the decedent spouse in fact characterizes these transactions as nontaxable exchanges, then the Wisconsin modifications should not be necessary. On the other hand, if federal income tax law characterizes these transactions as taxable exchanges, then the Wisconsin modifications are necessary to undo that result for Wisconsin income tax purposes.

#### **P. Wisconsin Income Tax: Effect of Marital Property Agreements or Unilateral Statements [§ 9.52]**

A number of specific provisions are included in the Wisconsin income tax statutes that diminish or negate the effect of marital property agreements under section 766.58 or unilateral statements under section 766.59 on the determination, assessment, or collection of income taxes. Section 71.10(6)(c) states, as a general proposition, that during any period that either or both spouses are not domiciled in Wisconsin, a marital property agreement or a unilateral statement under chapter 766 does not affect the determination of income that is taxable by Wisconsin, or the determination of the person who is required to report the income. Even for periods during which both spouses are domiciled in Wisconsin, a marital property agreement or unilateral statement is effective in the determination or reporting of income only if it is filed with the DOR before any assessment resulting from an audit is issued. The statute also requires the DOR to notify a taxpayer whose separate return is under audit that a marital property agreement or unilateral statement is effective only if it is filed with the DOR before any assessment is issued, and then only for any period during which both spouses are domiciled in Wisconsin. *Id.*

The DOR has stated that because it is not bound by a marital property agreement it has not received before issuing an assessment, spouses may

wish to send a copy of the agreement to the DOR when the agreement is executed. DOR Publ'n 113, *supra* § 9.6, at 16. The copy may be sent to the following address:

Wisconsin Department of Revenue  
Specialized Services Unit  
Mail Stop 5-144  
P.O. Box 8906  
Madison, WI 53708-8906

The DOR does not acknowledge the receipt of unsolicited agreements and does not review them. *Id.*

Section 71.10(6)(c) is intended to preclude the use of marital property agreements to shift otherwise taxable Wisconsin income to a spouse domiciled in another state. However, there are some problems with the statute. By its terms, it only circumscribes the effect of *marital property agreements* and does not appear to apply to marriage agreements between spouses entered into before the determination date that affect the property rights of either or both spouses. A marital property agreement is a creature of the Act, specifically section 766.58. The basic rule, set forth in section 766.03, is that the Act first applies to spouses upon their determination date, which, in the case of a nonresident married couple, will be the date on which both spouses are domiciled in Wisconsin. *See* Wis. Stat. § 766.01(5)(b). Thereafter, the Act continues to apply to the spouses “during marriage.” The term *during marriage* is limited to the period during which both spouses are domiciled in Wisconsin. It ends when one or both spouses are no longer domiciled in Wisconsin, at dissolution of the marriage, or at the death of a spouse. Wis. Stat. § 766.01(8). The Act ceases to apply when one of the spouses is no longer domiciled in Wisconsin. If the spouses have a premarital or postmarital agreement that is not a marital property agreement because it was executed at a time when the Act did not apply to them, it may fall outside the rather narrow language of section 71.10(6)(c).

A marital property agreement or unilateral statement under chapter 766 does not affect the requirements with respect to refunds or overpayments on a joint or separate return. Wis. Stat. § 71.75(6). Under section 71.75(8), a refund on a separate return is to be issued to the person who filed the return, while a refund payable with respect to a joint return is to be issued jointly to the spouses who filed the return.



A marital property agreement or unilateral statement also has no effect on the computation of “income,” “property taxes accrued,” or “rent constituting property taxes” for a person whose homestead is not the same as the homestead of his or her spouse. Wis. Stat. § 71.52(6), (7), (8). Similarly, a marital property agreement or unilateral statement under chapter 766 allocating income between spouses has no effect in computing the three-percent married persons’ credit on a joint return. Wis. Stat. § 71.07(6)(a).

A significant difference between the federal and Wisconsin treatment of marital property agreements is that, unlike the IRS, the DOR will recognize an agreement that allocates more than one-half of the marital property income to the nonearning spouse. DOR Publ’n 113, *supra* § 9.6, at 16. See sections 9.6 and 9.35, *supra*, for further discussion of the limitations placed on marital property agreements for federal income tax purposes.

A related issue involving the effect of marital property agreements is whether spouses, particularly spouses who are filing separate returns as the result of a divorce, may reclassify their income after the fact. Like the IRS, the DOR will not recognize a provision in a marital property agreement that attempts to retroactively reclassify income previously received, whether from marital property income to individual income or vice versa, and a court may also not order such a retroactive reclassification. DOR Publ’n 113, *supra* § 9.6, at 16, 18. This position finds support in a number of Wisconsin Supreme Court cases. See *Ladish Co. v. Department of Revenue*, 69 Wis. 2d 723, 233 N.W.2d 354 (1975); *Trepte v. Department of Revenue*, 56 Wis. 2d 81, 201 N.W.2d 567 (1972); *Webster v. Department of Revenue*, 102 Wis. 2d 332, 306 N.W.2d 701 (Ct. App. 1981). These cases hold that income taxes accrue as the events giving rise to them occur—that is, as the income is earned or generated.

For reasons discussed in section 9.35, *supra*, these precedents militate against spouses being able to retroactively reclassify income by marital property agreement to treat it differently than it would be treated under Wisconsin marital property law. This would preclude the use of divorce settlement agreements to alter the spouses’ respective income-reporting obligations for the portion of a tax year preceding the date of the divorce, if the recharacterization is contrary to ownership of the income under the Act. Conversely, a marital property agreement can have prospective effect on the classification of income for Wisconsin income tax purposes

for periods when both spouses are domiciled in the state, provided the agreement is filed with the DOR before an assessment is issued. *See* Wis. Stat. § 71.10(6)(c). Note that retroactive reclassification of income by marital property agreement is to be distinguished from the ability to reclassify the property into which the income has been invested. Reclassification of property clearly is permitted under sections 766.31(10) and 766.58(3)(a).

An issue may arise whether the DOR may collaterally attack on grounds of unenforceability a marital property agreement that it perceives as being unfavorable to it with respect to classifications for income tax or death tax purposes. Under section 766.58(6), only the spouse against whom enforcement is sought can raise defenses to enforceability. The rather limited language of section 766.58(6) appears to preclude such a collateral attack, unless it is shown that the agreement was a sham devised for fraudulent or illegal purposes.

### **Q. Wisconsin Income Tax: Minimum Tax on Tax-preference Items [§ 9.53]**

The 6.5% Wisconsin minimum tax in section 71.08(1) applies to married couples filing jointly. Wis. Stat. § 71.08(2). Spouses who file a joint income tax return are required to file a joint minimum tax return, and are jointly and severally liable for the tax, interest, penalties, fees, additions to tax, and additional assessments. *Id.*

## **III. Transfer Tax Considerations [§ 9.54]**

### **A. Federal Estate and Gift Tax: Generally [§ 9.55]**

In 2001, Congress passed the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, 115 Stat. 38 [hereinafter the 2001 Act], which made extensive changes to the federal estate and gift tax regime. Under the 2001 Act, the federal estate tax exemption was scheduled to gradually increase to \$3.5 million in 2009. I.R.C. § 2010(c). The 2001 Act further provides for the repeal of the federal estate tax in 2010. The federal gift tax, however, is not repealed, and the federal gift tax exemption is limited to \$1 million.

➤ **Comment.** For a brief discussion of the current uncertainty regarding estate tax law, see the “Note to Readers” accompanying chapter 10, *infra*.

The 2001 Act also provides that beginning in 2010, after the estate tax has been repealed, the rules in I.R.C. § 1014 (including the full basis step-up for community property under I.R.C. § 1014(b)(6)) providing for a basis adjustment for property acquired from a decedent will be repealed. Instead, a modified carry-over basis system will take general effect. Under this new system, recipients of property transferred at a decedent’s death will generally receive a basis for such property equal to the lesser of the decedent’s adjusted basis in the property or the fair market value of the property on the date of the decedent’s death. The 2001 Act, however, does allow for a \$1.3 million exemption from the carry-over basis rules that may be allocated to increase (i.e., *step up*) the basis in assets owned by the decedent by such amount. In addition, the basis of property transferred to a surviving spouse either outright or as QTIP can be increased by an additional \$3 million. Thus, the basis of property transferred to a surviving spouse can be increased by a total of \$4.3 million. I.R.C. § 1022.

To meet budget guidelines, *all* the provisions of the 2001 Act, including the repeal of the federal estate tax, are scheduled to sunset after 2010, when the federal estate tax law will revert to what it was before the enactment of the 2001 Act. Accordingly, attorneys are advised to keep abreast of future federal legislation that either makes the estate tax repeal and carry-over basis system permanent or enacts some other form of permanent estate tax.

The following sections generally focus only on situations in which the treatment of community property under the federal estate and gift tax laws differs materially from the treatment presently accorded common law forms of property ownership by spouses.

## **B. Federal Estate Tax: Valuation [§ 9.56]**

Under I.R.C. § 2031(a), the gross estate of a decedent is determined by including, to the extent required by the federal estate tax law, the value of all property owned by the decedent at the time of his or her death. The value of every item of property that is includible in the gross estate is its fair market value at the time of the decedent’s death, unless

the personal representative elects the alternate valuation method under I.R.C. § 2032, in which case the value is generally the fair market value at the alternate date. Treas. Reg. § 20.2031-1(b). For federal estate tax purposes, fair market value is defined as the price “at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts.” Treas. Reg. § 20.2031-1(b).

After several favorable court decisions, the applicability of a minority-interest discount for a deceased spouse’s one-half community property interest in property included in the decedent’s gross estate has become relatively well settled. See *Estate of Bright v. United States*, 658 F.2d 999 (5th Cir. 1981); *Estate of Lee v. Commissioner*, 69 T.C. 860 (1978). Moreover, it is also now clear that the interests in property held by a surviving spouse and a marital trust do not need to be aggregated for valuation purposes, so long as the surviving spouse is not granted a testamentary general power of appointment with respect to the trust. See *Estate of Bonner v. United States*, 84 F.3d 196 (5th Cir. 1996); *Estate of Mellinger v. Commissioner*, 112 T.C. 26 (1999); *Estate of Nowell v. Commissioner*, No. 19056-96, 1999 WL 30927 (U.S. Tax Ct. Jan. 26, 1999); *Estate of Lopes v. Commissioner*, 78 T.C.M. (CCH) 46 (1999);. But see *Estate of Fontana v. Commissioner*, 118 T.C. 318 (2002) (holding that interests in closely held stock held by surviving spouse and marital trust must be aggregated for valuation purposes because surviving spouse held testamentary general power of appointment over marital trust); Field Serv. Advisory 200119013 (May 11, 2001).

A minority-interest discount will typically be sought in valuing closely held stock in cases in which the decedent’s voting interest in the corporation is such that he or she alone cannot compel the declaration of dividends, force a liquidation of the corporation, or otherwise control the governance of the corporation. The minority-interest discount reduces the ratably determined per-share value of the stock to reflect that a buyer of the stock acquires only an interest in the capital of the corporation, but lacks the ability to control the yield on that investment or to liquidate the stock purchased. Conversely, in situations in which a shareholder’s stock ownership interest is large enough to exert control over the declaration of dividends, liquidation, and corporate policy, that block of stock will often be viewed as worth more than its ratably determined per-share value and be subject to a control premium for valuation purposes.

The same type of valuation issues also apply to the valuation of limited partnership interests, which will typically qualify for a minority-interest discount as a result of the inability of limited partners to participate in the management of the partnership. General partnership interests, however, may be subject to a control premium because of the ability of general partners to manage and control the affairs of the partnership.

The minority-interest discount issue can be illustrated as follows in the Wisconsin marital property context: a husband and wife own 70% of the outstanding voting stock in a closely held corporation as marital property. The husband dies, and one-half of the marital property interest (i.e., 35% of the outstanding voting stock of the company) is included in his estate. Standing alone, this 35% interest is a minority interest, and it seems clear that if the willing buyer/willing seller test prescribed by the IRS valuation regulations (Treas. Reg. § 20.2031-1(b)) is used, a minority-interest discount should apply.

Two significant court decisions—*Estate of Lee* and *Estate of Bright*—have confirmed that taxpayers can claim a minority-interest discount under facts like those in the foregoing example. These cases overruled the long-standing position of the IRS that had rejected a minority-interest discount when the stock in a closely held corporation was owned by spouses or members of a harmonious family, and instead valued as a block all stock held by family members. Under the IRS position, instead of owning a 35% minority interest, a decedent in the above example would own half of a 70% controlling interest and would not be entitled to a minority-interest discount (and perhaps could even be subject to a control premium).

The former position of the IRS on this issue was stated in Revenue Ruling 81-253, 1981-2 C.B. 187, 188, as follows: “[O]rdinarily no minority-interest discount will be allowed with respect to transfers of stock among family members where, at the time of transfer, control (either majority voting control or de facto control) of the corporation exists in the family.” The rationale is that “where a controlling interest in stock is owned by family members, there is a unity of ownership and interest, and the shares owned by family members should be valued as part of that controlling interest.” *Id.*

In Revenue Ruling 93-12, 1993-1 C.B. 202, however, the IRS reversed its position by revoking Revenue Ruling 81-253 and stated that

it will follow *Estate of Bright* and *Estate of Lee* in cases involving a corporation with a single class of stock. Notwithstanding the family relationship of the donor, donee, and other shareholders, the IRS stated it would not aggregate the shares of the other family members with the transferred shares to determine whether the transferred shares should be valued as part of a controlling interest. Consequently, a minority-interest discount will not be disallowed solely because a transferred interest, when aggregated with interests held by family members, would be part of a controlling interest.

The discounting of fractional community property interests has also been applied to real estate. Specifically, in *Propstra v. United States*, 680 F.2d 1248 (9th Cir. 1982) (applying Arizona law), the court held that a fractional-interest discount was allowable for a decedent's one-half community property interest in real estate, because an undivided fractional interest in property typically will sell for less than the proportionate share of the fair market value of the whole. In *Propstra*, the IRS once again took the position that to qualify for the fractional-interest discount, the taxpayer must demonstrate that it is likely that the decedent's interest will be sold apart from the survivor's interest. The court, however, reconfirmed its rejection of this unity-of-ownership or family-attribution approach to valuation, noting that there was no direct congressional sanction for it. Accordingly, a fractional-interest discount should be available for any parcel of marital property real estate owned by a Wisconsin married couple because the ownership of such real estate is by definition fractionalized into equal shares between the spouses. *But see Estate of Young v. Commissioner*, 110 T.C. 297 (1998) (holding fractional-interest discount did not apply to a deceased spouse's interest in California real estate held in joint tenancy and not as community property, even when only one-half of value of real estate was included in decedent's gross estate because contributions of surviving spouse for other half of property could be traced).

Minority-interest valuation discount opportunities of the type discussed in this section can be expected to arise with respect to married Wisconsin decedents who own a marital property interest in stock of a closely held business, in a limited partnership, in real estate, or in other nonliquid assets. The estate of the first spouse to die should be entitled to a minority-interest or fractional-interest discount without being confronted with claims by the IRS of family attribution or unity of ownership.

Until recently, the IRS had also unsuccessfully attempted to apply an attribution or unity-of-ownership type theory to stock taxable in the estate of a surviving spouse, valuing as a single interest a block of stock owned outright by the surviving spouse (and includible in the spouse's estate under I.R.C. § 2033) and a block held in a QTIP marital trust for the benefit of the surviving spouse (and includible in the spouse's estate under I.R.C. § 2044). In four separate cases, however, the courts have rejected this position and instead ruled that interests held in a QTIP marital trust cannot be aggregated by the IRS for estate tax valuation purposes with interests owned outright by a surviving spouse at death.

This issue first presented itself in *Estate of Bonner*, in which the Fifth Circuit Court of Appeals rejected the aggregation theory put forth by the IRS. In this case, Bonner died owning a 62.5% interest in a ranch, a 50% interest in other real property, and a 50% interest in a pleasure boat. The remaining interests in these assets were owned by a QTIP marital trust that had been established for his benefit by his deceased wife. Bonner's estate applied fractional-interest discounts of 45% to both the interests owned by the marital trust and those owned by Bonner individually. The IRS disallowed the discounts, claiming that the undivided interests owned by Bonner and by the QTIP marital trust should be aggregated (or merged) for valuation purposes. When aggregated, Bonner's estate owned 100% of each of the three assets, thus making fractional-interest discounts unavailable and increasing the size of his taxable estate.

The court rejected the IRS's aggregation argument and concluded that the reasoning of *Estate of Bright*, which held that no family attribution should be applied in valuing undivided community property interests, also controlled in this instance. The court noted that Mr. Bonner did not control a 100% interest in the assets. Instead, he controlled only the fractional interest in each asset that he individually owned. The trustee of the QTIP marital trust controlled the balance of the assets. Furthermore, the terms of the trust, not Mr. Bonner, controlled the disposition of the assets held in the marital trust upon his death. Thus, the court reasoned that Mr. Bonner was not in the position of a hypothetical willing seller of 100% interests for valuation purposes, because he could not have voluntarily transferred such an interest in each asset. Accordingly, the court held that the "valuation of the assets should reflect that reality" and the IRS could not aggregate the QTIP marital trust assets with Mr. Bonner's own assets for valuation purposes.

The court also rejected the public policy argument put forth by the IRS that if the court allowed Mr. Bonner's estate to take a fractional interest discount, it would condone using QTIP marital trusts as a tax-avoidance technique. The court instead commented that public policy actually supported the estate's position because two transfers were essentially taxed upon Mr. Bonner's death. The first was the transfer by Mr. Bonner of the fractional interests he owned individually. The second was the transfer by his previously deceased wife of the fractional interests remaining in the QTIP marital trust that was completed at his death. Contrary to the IRS's claim that allowing the discounts would violate public policy, the court noted that public policy required that "each decedent should be required to pay taxes on those assets whose disposition that decedent directs."

Three subsequent Tax Court cases, all citing the *Bonner* case, have also refused to follow the IRS's aggregate approach. In *Estate of Mellinger*, the decedent's husband, the founder of Frederick's of Hollywood, left his community property interest in his publicly traded Frederick's stock, representing a 27.87% interest in the company, to a QTIP marital trust for the benefit of the decedent. At her death, the decedent's revocable trust also held an identical 27.87% interest in Frederick's stock representing her community property interest in the stock. The trustees of the marital trust and the revocable trust were the same. The decedent's estate tax return reported the 27.87% blocks held by the marital trust and the revocable trust separately and claimed a blockage discount for each block (to account for the fact that the size of each block was so large that it could not be liquidated without depressing the market). The IRS denied the discount and instead argued that the stock should be valued as an aggregate 55.74% controlling block and subject to a control premium.

In support of its position in *Estate of Mellinger*, the IRS argued that when the QTIP concept was passed by Congress in the form of I.R.C. § 2044, it did not intend to alter the estate tax treatment that would otherwise arise if a decedent left property outright to his or her surviving spouse. The Tax Court, however, rejected this argument and refused to value the stock held in the revocable trust and the marital trust as an aggregate block. The court observed that there was no congressional indication that section 2044 mandated identical tax consequences for a QTIP marital trust and an outright transfer to a surviving spouse. The court further concluded that section 2044 is an inclusion section only, and not a valuation section.



On the same day it issued the *Estate of Mellinger* decision, the Tax Court also decided *Estate of Nowell*, a case in which partnership interests were divided between two QTIP marital trusts and a revocable trust created by the surviving spouse. Significantly, the surviving spouse was granted a testamentary limited power of appointment over both marital trusts and in fact exercised the powers. Consistent with its analysis in *Estate of Mellinger*, the court concluded that the partnership interests in the revocable trust and the two marital trusts could not be aggregated by the IRS for valuation purposes.

The Tax Court also followed its decision in *Estate of Mellinger* in *Estate of Lopes*, which involved fractional interest discounts for real estate held in two separate trusts, the surviving spouse's revocable trust and a QTIP marital trust. Pursuant to a trust agreement between the decedent and her husband, the decedent's community property interest in 21 separate California ranch properties had been placed in a survivor's trust for her benefit, while her predeceased husband's community property interest in the properties had been placed in the marital trust. Following its decision in *Estate of Mellinger*, the court concluded that there was nothing in I.R.C. § 2044 or the accompanying legislative history indicating that Congress intended QTIP property that is included in a decedent's estate pursuant to I.R.C. § 2044 to be treated as if the decedent actually owned that property for aggregation purposes.

In Action on Decision 1999-006 (Aug. 30, 1999), the IRS gave up the fight on its aggregation theory and acquiesced to the Tax Court's decision in *Estate of Mellinger*. In its action on decision, however, the IRS cautioned that proper funding of a QTIP marital trust should reflect the discounted value of minority interests in closely held entities or fractional interests in real estate that are used to satisfy the bequest to the marital trust.

The rejection of the IRS's aggregation theory means that in structuring a married couple's estate before the death of one of the spouses, a very important strategy that should be taken into consideration is whether to use a bequest to a QTIP marital trust, rather than an outright gift to the surviving spouse, to take advantage of valuation discounts in the surviving spouse's estate for estate tax purposes. The discounting advantages that can be obtained by using a QTIP marital trust should be available, even if the surviving spouse is named as sole trustee of the marital trust, because of fiduciary duties inherent in the position of trustee and the surviving spouse's lack of ultimate disposition

of the trust assets upon his or her death. It appears that the surviving spouse can even be granted a limited testamentary power of appointment over the marital trust without negatively affecting the potential discount. If subsequent case law, however, were to hold that the surviving spouse serving as a trustee or the surviving spouse having a limited power of appointment would endanger the discount, the surviving spouse could always disclaim the power of appointment and resign as trustee.

➤ **Comment.** Significantly, the IRS's acquiescence in Action on Decision 1999-006 makes no reference to the surviving spouse's lack of control over the QTIP marital trust. Instead, the IRS simply states that "we agree with the Tax Court's opinion that closely held stock held in a QTIP trust should not be aggregated, for valuation purposes, with stock in the same corporation held in a revocable trust and includible in the decedent's gross estate." The Fifth Circuit's decision in *Estate of Bonner* discussed the surviving spouse's lack of control over the marital trust assets, but provided little insight as what terms could be included in the trust and still achieve a discount. The fact that the surviving spouse held and exercised a testamentary limited power of appointment in *Estate of Nowell*, and the omission of any reference to the control issue in the IRS's acquiescence to *Estate of Mellinger*, would seem to indicate that a discount should apply regardless of the terms of the QTIP marital trust or the degree of control left to the surviving spouse over the assets of the marital trust.

A recent field service advisory issued by the IRS also confirms that granting a surviving spouse a testamentary limited power of appointment over a QTIP marital trust will not cause aggregation to apply. Specifically, in Field Service Advisory 200119013 (May 11, 2001), the IRS advised that it would aggregate the interests held by a surviving spouse and a QTIP marital trust when the surviving spouse holds a testamentary *general* power of appointment over the marital trust. However, the IRS also acknowledged that the decedent in *Estate of Nowell* held a testamentary limited power of appointment and noted that the Tax Court did not take this power into account in finding that aggregation did not apply. The advisory goes on to instruct that even a broad limited power of appointment should not require aggregation, specifically stating the following:

We recognize that in some situations a limited power of appointment may afford the holder broad powers of disposition. However, the power holder

would not, in any event, be authorized to appoint the property to his or her estate (or his or her creditors) as is the situation presented with a general power.... Given the nature of a limited power, and the fact that a limited power is not recognized for estate and gift tax purposes as affording the power holder sufficient control to generate any transfer tax consequences when possessed or exercised, the court in *Estate of Nowell* was justified in treating a QTIP trust subject to a limited power in the same manner as a QTIP trust where the remainder beneficiaries are designated by the first spouse to die.... It does not follow that the same result should obtain in this case where the Decedent possessed a general power of appointment.

In *Estate of Fontana v. Commissioner*, 118 T.C. 318 (2002), the Tax Court agreed with the IRS's position that aggregation applies when the surviving spouse has a general power of appointment over the marital trust. Specifically, the court held that stock owned by the surviving spouse individually at death must be aggregated with stock held in a general-power-of-appointment marital trust for valuation purposes and that no discount applies. The court focused on the surviving spouse's ability to control the ultimate disposition of the stock held in the marital trust and concluded that such power was the equivalent of outright ownership for valuation purposes. Accordingly, the court reasoned that the general power of appointment made the case distinguishable from *Estate of Mellinger*, because the property in a QTIP marital trust is not subject to the surviving spouse's unrestricted power of disposition.

➤ **Comment.** The rejection of the aggregation theory means that the IRS may pay more attention, especially in community property states, to the values assigned to property at the first spouse's death. The concern of the IRS would be to ensure that appropriate discounts are applied to minority interests in closely held businesses and fractional interests in real estate, so that such interests are not overvalued in order to obtain an excessive step-up in basis for such interests at the first death. Alternatively, if it were determined that appropriate discounts were not applied at the first spouse's death the IRS might argue that a "duty of consistency" applies at the surviving spouse's death, which would require that the same valuation approach applying no discounts would have to be used in valuing property included in the surviving spouse's estate. Accordingly, careful consideration of applicable discounts should be taken into account when making valuation decisions for property included in the estate of the first spouse to die.

### **C. Federal Estate Tax: Special Use Valuation of Certain Farm and Closely Held Business Real Property**

#### **[§ 9.57]**

Under I.R.C. § 2032A, real estate used for farming or in a closely held business is subject to special valuation rules for estate tax purposes. A specific provision in I.R.C. § 2032A(e)(10) provides that if qualified real property for purposes of the special valuation rules is held by the decedent and his or her surviving spouse as community property, the interest of the surviving spouse must be taken into account to the extent necessary to provide a result that is consistent with the result that would have been obtained if the property had not been community property.

Revenue Ruling 83-96, 1983-2 C.B. 156, interpreted the purpose of this provision as ensuring the same special-use-valuation treatment for qualified community property as that accorded to qualified property owned in a common law jurisdiction. The revenue ruling pointed out that the result is achieved by treating a decedent's community property interest as though owned by the decedent as an individual. Accordingly, the decedent's one-half community property interest is treated as analogous to a common law decedent's interest in a tenancy in common between the spouses, or a tenancy by the entireties. The revenue ruling pointed out that this treatment applies regardless of the actual amount a spouse contributes toward acquisition of the qualified real estate. Moreover, the entire-value-reduction limitation in I.R.C. § 2032A(a)(2) (and not merely one-half) would be permitted against the community property interest. Thus, the decedent's one-half interest is includible in the gross estate, and the full-reduction-limitation is available against that interest.

The special rule for community property provided for under I.R.C. § 2032(A)(e)(10) is important in Wisconsin for federal estate tax purposes, because only one-half of qualifying marital property real estate used in farming or for a closely held business will be includible in the adjusted value of the gross estate for purposes of determining whether special use valuation is available.

In Technical Advice Memorandum 8926002 (June 30, 1989), the IRS advised that a surviving spouse who is not the devisee of the decedent's community property interest in special-use-valuation property is not required to execute a tax-recapture agreement with respect to the

property in a community property jurisdiction. The ruling involved a decedent who willed his community property interest in a ranch to his son and grandson. Other assets were left to his wife. Because the wife was not the devisee of the decedent's community property interest, the ruling indicated that it was not necessary for her to execute the tax-recapture agreement required under I.R.C. § 2032A(d). As a tenant in common with the decedent's estate following his death, the surviving spouse did not have an interest in the decedent's former community property interest that was subject to special-use valuation. Accordingly, it was sufficient that the decedent's son and grandson executed the tax-recapture agreement. This rule also would apply in Wisconsin for special-use valuation of a decedent's marital property interest in real estate used for farming or in a closely held business.

#### **D. Federal Estate Tax: Gross Estate [§ 9.58]**

Neither the Internal Revenue Code nor the Treasury regulations contain specific provisions for the estate taxation of community property. Accordingly, only one-half of the value of each item of community property is includible in a deceased spouse's gross estate under the general provisions of I.R.C. § 2033, since that is the property interest owned by the decedent. Wis. Stat. § 766.31(3); *Lang v. Commissioner*, 304 U.S. 264 (1938). This rule holds true even in cases in which a surviving spouse acquiesces to the deceased spouse's attempt to dispose of the survivor's interest in community property, and permits his or her one-half of the community property assets to pass under the will or trust of the deceased spouse in a forced-election estate plan. The rule also holds true when a decedent's will authorizes the personal representative to enter into an agreement with the decedent's spouse providing for a division of the community property assets that is not pro rata but equal in total value. Tech. Adv. Mem. 8505006 (Oct. 19, 1984).

The treatment of Wisconsin deferred marital property for federal estate tax purposes has been discussed in detail in conjunction with the full-adjustment-in-basis rule. *See supra* § 9.27. The augmented deferred marital property elective right in section 861.02 grants a surviving spouse the right to elect up to one-half of the value of certain defined predetermination date assets owned by the deceased spouse that would have been marital property assets had the assets been acquired after the determination date; provided these elective rights are conditional on the survivorship of the electing spouse. The decedent's ownership of

deferred marital property assets is not affected until his or her death occurs and an election is made by the surviving spouse. Accordingly, the full value of deferred marital property assets will be included in the gross estate of the owner spouse. *See Estate of Sbicca*, 35 T.C. 96 (1960) (California quasi-community property was fully includible in deceased owner's gross estate). Similarly, since the interest of a nonowner in deferred marital property assets is merely an elective right that does not ripen until the death of the owner spouse, no portion of such assets are includible in the estate of a nonowner spouse who predeceases the owner.

For purposes of preparing the deceased spouse's federal estate tax return (Form 706), the marital property interests of the deceased spouse, valued at one-half of the total value of each item of property, should simply be listed like other property on Schedules A through I, as appropriate. The treatment of one-half of each item of property as belonging to the decedent is mandated by sections 861.01 and 766.31(3). For example, if the first spouse to die owned a marital property interest in 100 shares of Microsoft stock, the appropriate entry on Schedule B of the federal estate tax return would be as follows:

An undivided one-half ( $\frac{1}{2}$ ) marital property interest in 100 shares of Microsoft Corp. common stock

and not

50 shares of Microsoft Corp. common stock.

In preparing federal estate tax returns, the preparer must be aware of the presumption in subsections 766.31(1) and (2) that all property of a Wisconsin married couple is marital property and of the related rule in section 766.63(1) that mixed property is reclassified as marital property unless the nonmarital portion can be traced. These statutory provisions require that the personal representative classify assets as marital property unless the contrary can be demonstrated.

To achieve a full basis adjustment for both the decedent's and the surviving spouse's one-half share of community property under I.R.C. § 1014(b)(6), at least one-half of the whole of the community interest in the property must be includible in determining the value of the decedent's gross estate for federal estate tax purposes. Because of the obvious advantages of the full basis adjustment in reducing capital gains

taxes on future dispositions of appreciated assets, Wisconsin fiduciaries may be tempted simply to rely upon the presumption in section 766.31(2) and treat all assets of the first spouse to die as marital property. Such a strategy, however, is inappropriate. In the context of joint-tenancy property under prior law, when inclusion in the decedent's gross estate depended on the amount of consideration for the purchase price furnished by the decedent, the tax court held that proof of contribution cannot be withheld by the survivor to purposely include part or all of the property in the decedent's gross estate to receive a stepped-up basis. *See, e.g., Madden v. Commissioner*, 52 T.C. 845 (1969), *aff'd*, 440 F.2d 784 (7th Cir. 1971). Similarly, evidence of predetermination date acquisition, acquisition with assets other than marital property, acquisition by gift or inheritance, or similar facts demonstrating a classification as other than marital property must be considered by Wisconsin fiduciaries.

It should be kept in mind that the IRS is aware of this issue and may attempt to verify the classification of property included in a federal estate tax return as marital property when reviewing the return. Accordingly, Wisconsin fiduciaries filing federal estate tax returns should use reasonable diligence in attempting to establish the appropriate classifications of a married decedent's assets for purposes of preparing the return. In particular, assets that were demonstrably acquired before the spouses' determination date normally will not be classified as marital property, unless a marital property component arose through application of mixing and tracing principles, or unless the asset were reclassified as marital property by marital property agreement, gift, or other method sanctioned by the Act.

### **E. Federal Estate Tax: Transfers Within Three Years of Decedent's Death [§ 9.59]**

Under I.R.C. § 2035(a), the gross estate of a decedent includes certain transfers that are not made for a full and adequate consideration and that are carried out within the three-year period ending on the date of the decedent's death. Among the transfers falling within this three-year recapture rule are transfers under life insurance policies on the life of the decedent with respect to which the decedent possessed incidents of ownership under I.R.C. § 2042. A series of cases have made it clear, however, that I.R.C. § 2035(a) will not apply to a life insurance policy insuring a decedent's life if the policy is owned by a spouse or a third

party and the decedent's only relationship to the policy is the direct or indirect payment of premiums. The courts have held that I.R.C. § 2035(a) will not apply in these situations because the decedent did not possess any incidents of ownership in the policy. *Estate of Perry v. Commissioner*, 927 F.2d 209 (5th Cir. 1991), *aff'd* 59 T.C.M. (CCH) 65 (1990) (holding that policy purchased by decedent's three sons within one year of his death with premiums paid by decedent was not includible); *Estate of Headrick v. Commissioner*, 93 T.C. 171 (1989), *aff'd*, 918 F.2d 1263 (6th Cir. 1990) (holding that policy owned by irrevocable insurance trust with premiums paid by decedent who died within three years of policy purchase was not includible); *Estate of Leder v. Commissioner*, 89 T.C. 235 (1987), *aff'd*, 893 F.2d 237 (10th Cir. 1989) (holding that policy purchased by decedent's wife within three years of his death with premiums paid directly by the decedent's wholly owned corporation was not includible).

Under section 766.61(3)(c), ownership and proceeds of a life insurance policy owned by one spouse on the other spouse's life are the individual property of the owner spouse, regardless of the classification of the property used to pay premiums. In *Estate of Leder*, the court relied on a similar rule in Oklahoma that the insured's payment of premiums does not, in itself, create in the insured any interest in the insurance policy. Without any incidents of ownership in the policy, the same result should apply in Wisconsin by virtue of section 766.61(3)(c) with respect to life insurance policies owned by one spouse on the other spouse's life.

## **F. Federal Estate Tax: Transfers with a Retained Life Estate [§ 9.60]**

### **1. In General [§ 9.61]**

Under I.R.C. § 2036(a), all property that a decedent transferred during his or her lifetime, but in which the decedent retained certain rights or interests for life, are included in the decedent's gross estate. Specifically, this provision reaches

the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust



or otherwise, under which he has retained for his life ... the possession or enjoyment of, or the right to the income from, the property.

*Id.* By its terms, the statute applies to both outright transfers and transfers in trust.

The corollary to unintended grantor problems for income tax purposes, discussed in section 9.34, *supra*, is the unintended retained interest for federal estate tax purposes.

➤ **Example.** A wife created an I.R.C. § 2503(c) minority trust for the benefit of a child, using assets thought to consist entirely of the wife's individual property, but in fact consisting partially of marital property. The husband is the trustee of the minority trust and has the power to accumulate or distribute the income to or for the benefit of the beneficiary.

Under I.R.C. § 2036(a), the husband's power to accumulate the income of the trust for the benefit of the child will constitute a use, possession, or other enjoyment as to the portion of the trust he is deemed to have transferred—that is, one-half of the marital property component. This component, plus the accumulated income thereon, will be included in the husband's estate unless the trust terminates or the husband resigns his position as trustee at least three years before the wife's death so that I.R.C. § 2035(a) is avoided. *See also Thompson v. United States*, 79-1 U.S.T.C. (CCH) ¶ 13,294 (C.D. Cal. 1979) (holding that extensive reserved powers over trust income resulted in inclusion in grantor's estate of one-half of corpus of trust created with community property).

Another example of the problem is found in *Estate of Hoffman v. Commissioner*, 78 T.C. 1069 (1982). In that case, the net income from all the community property subject to administration (and not just the decedent's half) was erroneously distributed to the residuary trust. The surviving spouse was a life income beneficiary of this trust, and the children took the remainder. The tax court held that the portion of the residuary trust represented by the over funding of probate income from the estate was includible in the surviving spouse's estate as a transfer with a retained life estate under I.R.C. § 2036(a).

## 2. Income Interest Arising by Statute [§ 9.62]

Texas, Louisiana, and Idaho are community property states with a “civil law” income rule that affords community treatment to income from separate property. *See supra* § 2.39. Wisconsin follows a similar rule, and section 766.31(4) treats the income from all property, including individual and predetermination date property, as marital property.

In community property states with an income rule of this kind, retained life estate problems can arise under I.R.C. § 2036(a) when gifts of income-producing marital property assets are made either in trust or outright by one spouse to the other, because at least part of the income interest in the gifted property may be deemed to be retained by the donor. This may be less of an issue in Wisconsin than elsewhere. First, the marital property interest in income from property is capable of being reclassified by marital property agreement, gift, conveyance, written consent with respect to life insurance, or unilateral statement. Wis. Stat. § 766.31(10). Furthermore, section 766.31(10) affirmatively states that if a spouse gives property to the other spouse and intends at the time of the gift that the property be the individual property of the donee spouse, the income from the property will also be the individual property of the donee spouse unless the donor spouse’s contrary intent regarding the classification of income is established. Absent evidence of a contrary intent on the part of the donor, the gift of property to the donee spouse should carry the income interest in the property with it, and the retained life estate rule of I.R.C. § 2036(a) will not come into play.

Application of I.R.C. § 2036(a) to situations in which a state law community property interest continued in income from property given to a spouse has been considered in a number of cases. *See Estate of Wyly v. Commissioner*, 610 F.2d 1282 (5th Cir. 1980), *rev’g* 69 T.C. 227 (1977); *Estate of Castleberry v. Commissioner*, 68 T.C. 682 (1977). *Estate of Wyly* involved a husband and wife’s irrevocable gift of community property stock to a trust that provided income to the wife for life and a remainder interest to the couple’s grandchildren. *Estate of Castleberry* involved an outright lifetime gift of a husband’s one-half community property interest in certain municipal bonds to his wife. In both cases, the IRS sought to include a one-half community property interest in the transferred property in the gross estate of the deceased husband. In neither case had the deceased husband voluntarily retained any interest in the gifted assets. In fact, the donors in these cases did everything they could to “transfer the totality of their interest and control.” *Estate of*

Wylly, 610 F.2d at 1293. However, when these cases arose, state law conferred upon each donor spouse a virtually indestructible community property interest in the income from the separate property of the donee spouse. The question before the court was whether this income interest, which arose by operation of state law, amounted to a retained right to income for purposes of I.R.C. § 2036(a).

The court first noted that the Texas community property interest of a spouse in the income from the separate property of the other spouse is a “special community” that confers no management and control rights in the spouse who does not own the underlying property. It further noted that the nonmanaging spouse has only limited and inchoate rights to complain of fraud on his or her interest, or to seek an accounting of such income upon dissolution of the marriage if the income is used to improve the other spouse’s separate estate. The court contrasted these minimal remedies with the managing spouse’s absolute power to dispose of the principal asset itself. Accordingly, the court concluded that the community property interest that arose under Texas law in the income of the transferred property was “so limited, contingent and expectant that it does not amount to a ‘right to income’” within the purview of I.R.C. § 2036(a). *Estate of Wylly*, 610 F.2d at 1295.

In accord is *Estate of Deobald v. United States*, 444 F. Supp. 374 (E.D. La. 1977). *Estate of Deobald* involved an additional factor: Louisiana civil law permitted the donee spouse to declare all income from the gift to be the donee’s separate property, but the donee had not elected to do so. The donor, however, had taken all possible steps to divest himself of the gift.

In Revenue Ruling 81-221, 1981-2 C.B. 178, the IRS concurred with the interpretation of Texas law in *Estate of Wylly*. The revenue ruling noted that the income interest that arose in the donated property was not a general community interest subject to joint management and control. The right was inchoate and could be asserted only in the event of fraud and thus was a mere expectancy.

The foregoing analysis suggests that gift transfers between Wisconsin spouses should be documented to make sure that the right to receive future income is expressly included along with the underlying gifted property in the instrument making the gift, or in a memorandum memorializing the terms of the gift, so that the full weight of the income classification provisions in section 766.31(10) is available. The gift

documents should specifically be free of any language that could serve to establish a contrary intent on the part of the donor spouse to retain an interest in the income on the gifted property.

### **3. Forced-election and Voluntary-election Estate Plans [§ 9.63]**

A *forced-election* estate plan of the kind described in section 10.181, *infra*, also has implications under I.R.C. § 2036(a). Under a forced-election estate plan, the deceased spouse in effect attempts to dispose of by will all of the community property assets (both the decedent's one-half and the surviving spouse's one-half), typically leaving the survivor with a life income interest in the whole. The deceased spouse provides that if the surviving spouse elects not to have this happen—that is, elects simply to take his or her one-half of the community assets outright—then the assets remaining subject to the decedent's will are disposed of as though the surviving spouse had predeceased. This effectively cuts the survivor entirely out of any interest in the deceased spouse's one-half of the community property (as well as the decedent's other property) if he or she elects against the will.

The surviving spouse's election to go along with the will means, in effect, that he or she gives up the remainder interest in his or her half of the community property assets in exchange for a life income interest in the decedent's one-half, a transaction that can have income tax consequences. *See supra* § 9.19. It also can have transfer tax consequences in situations in which the consideration received by the surviving spouse for giving up the remainder interest is inadequate. Because the surviving spouse has given up his or her half of the community property assets, but retained a life income interest in that half, this share of the community property assets will be brought back into his or her estate under I.R.C. § 2036(a), valued at the time of the survivor's death. The value of the one-half interest brought back into the survivor's estate is, however, subject to reduction under I.R.C. § 2043(a) for the value of the consideration received—that is, the present value of the life estate in the first spouse's one-half of the community property assets at the time of the exchange. *Estate of Christ v. Commissioner*, 480 F.2d 171 (9th Cir. 1973); *United States v. Gordon*, 406 F.2d 332 (5th Cir. 1969); *Estate of Vardell v. Commissioner*, 307 F.2d 688 (5th Cir. 1962); *Whiteley v. United States*, 214 F. Supp. 489 (W.D. Wash. 1963). For further discussion of the valuation of property includible in the survivor's

estate under I.R.C. § 2036(a), when the transfer with a retained interest is made for an inadequate consideration, see section 9.72, *infra*.

In *Gradow v. United States*, 11 Cl. Ct. 808 (1987), *aff'd*, 897 F.2d 516 (Fed. Cir. 1990), the issue was what portion of the surviving spouse's one-half interest in community property transferred to a trust created under her deceased husband's will should be taken into account in determining whether there was "adequate and full consideration in money or money's worth" under I.R.C. § 2036(a) for the life income interest she received in the husband's assets placed in the same trust. If the consideration was determined to be adequate, then I.R.C. § 2036(a) would not apply, and the community property interests transferred by the surviving spouse would not be includible in the surviving spouse's gross estate for federal estate tax purposes.

More specifically, the question was whether the consideration deemed to have been transferred by the wife should be measured by the value of her *remainder* interest in the community property (since she was retaining a life income interest in that property) or by the full, undiminished value of her one-half interest in the community property. The result in the case hinged on that determination, since the value of the life estate the surviving spouse received in the husband's assets was conceded to be lower than the value of her full one-half interest in the community property assets transferred to the trust but greater than the value of the remainder interest in those same assets. The court held that for the purpose of evaluating whether the surviving spouse's acquiescence in the forced election constituted full and adequate consideration within the meaning of I.R.C. § 2036(a), the consideration flowing from the surviving spouse consisted of the property that otherwise would have been included in her gross estate by virtue of her retention of a life estate—in other words, her full one-half interest in the community property and not just her remainder interest. Because the life estate the wife received was not adequate consideration to support the transfer of her full one-half interest in the community property to the husband's trust, the full value of the spouse's community property interest transferred to the trust was includible in her estate under I.R.C. § 2036(a). For a discussion of the IRS's approval of the valuation principles declared in *Gradow*, see Private Letter Ruling 8929046 (July 21, 1989).

The *Gradow* court's full-and-adequate-consideration analysis was harshly criticized by the Third Circuit Court of Appeals in *Estate of*

*D'Ambrosio v. Commissioner*, 101 F.3d 309 (3rd Cir. 1996), *rev'g* 105 T.C. 252 (1995). Reasoning that the *Gradow* analysis would make the sale of a remainder interest for full and adequate consideration within the meaning of I.R.C. § 2036(a) virtually impossible, the Third Circuit held that the sale of a remainder interest in property for an amount equal to its actuarial fair market value as of the date of sale will effectively remove the property from a decedent's gross estate for purposes of I.R.C. § 2036(a).

Although *Estate of D'Ambrosio* did not involve a widow's election, the Third Circuit did not hesitate to find that there is no reason why a court's analysis of a widow's election transaction should not compare the actuarial (date-of-election) value of the remainder interest transferred to the actuarial (date-of-election) value of the life estate received by the surviving spouse. The court went on to analyze in detail why a surviving spouse's sale of the remainder interest in his or her share of the community property for its actuarial fair market value would not be a tax-avoidance device as suggested by the *Gradow* court.

Applying its actuarial analysis, the *Estate of D'Ambrosio* court reasoned that whether the surviving spouse keeps the half share of community property or sells the remainder interest in the property for its actuarial fair market value, the same amount of property will be included in the surviving spouse's gross estate at death. According to the court, this result follows because if the surviving spouse's income or life interest is insufficient, he or she will have to invade principal or the consideration received for the remainder interest to the same extent. Accordingly, the court concluded there is no change in the date-of-death value of the surviving spouse's final estate, regardless of whether he or she elects against the deceased spouse's will or surrenders his or her share of the community property in return for a life interest in the whole.

Conversely, the *Estate of D'Ambrosio* court asserted that if the full value of the surviving spouse's one-half interest in the community property is included in his or her gross estate at death under I.R.C. § 2036(a), subject only to a reduction under I.R.C. § 2043(a) for the consideration received (i.e., the value of the life interest in the deceased spouse's estate), then all of the postsale appreciation on his or her share of the community property will be included in his or her taxable estate upon death. In fact, the court advised that the surviving spouse would in effect be double taxed, because the consideration received will also have appreciated and be subject to tax at its increased value.

The Fifth Circuit also analyzed *Gradow* in detail in *Wheeler v. United States*, 116 F.3d 749 (5th Cir. 1997), another case that was not a widow's election case but involved the sale of a remainder interest in property by a father to his sons. While the Fifth Circuit found the Third Circuit's analysis in *Estate of D'Ambrosio* persuasive, it concluded "that the widow election cases present factually distinct circumstances that preclude the wholesale importation of *Gradow's* rationale" for cases involving sales of remainder interests. Nevertheless, the *Wheeler* court arrived at the same conclusion as the Third Circuit, holding that the sale of a remainder interest for its actuarial fair market value is a sale for full and adequate consideration for purposes of I.R.C. § 2036(a).

In *Estate of Magnin v. Commissioner*, 184 F.3d 1074 (9th Cir. 1999), *rev'g and rem'g* 71 T.C.M. (CCH) 1856 (1996), the Ninth Circuit also adopted the view of the Third and Fifth Circuits, holding that "adequate and full consideration" should be measured against the actuarial value of the remainder interest, rather than by the full fee-simple value of the property transferred by the decedent.

The Seventh Circuit Court of Appeals has not yet weighed in on the *Gradow* analysis, so it is not clear what rule applies in Wisconsin for purposes of valuing a remainder interest. Given the unanimous view of the other circuit courts of appeal that have reviewed the issue, however, a well-reasoned argument can be presented that the *Gradow* court was wrong in its analysis, even in the context of the widow's election, and that the proper measure of whether full and adequate consideration has been received by a surviving spouse for purposes of I.R.C. § 2036(a) should be based on a comparison of the actuarial fair market value of the life estate received, as compared to the actuarial value of the remainder interest transferred.

➤ **Note.** The gift tax implications to forced-election plans are discussed in detail in section 9.97, *infra*.

A voluntary-election estate plan of the sort discussed in section 10.182, *infra*, creates no serious income tax complications, but it potentially does involve retained-life-estate difficulties under I.R.C. § 2036(a). Typically, this will occur if the surviving spouse voluntarily consents to contribute his or her half of the community property to a trust created under the deceased spouse's estate plan that provides the surviving spouse with income from the trust assets for life and vests a remainder in third parties.

Joint wills operate much like forced-election estate plans in terms of their tax consequences under I.R.C. § 2036(a). Some of the issues are illustrated in Technical Advice Memorandum 9431004 (Apr. 26, 1994), which involved a community property ranch and other property that were subject to a joint will. The joint will gave the surviving husband extensive management and control powers with respect to the ranch, including the power to mortgage or encumber any part of the real estate, and the authority to execute mineral leases on any part of the ranch. Upon his first wife's death in 1965, the joint will was offered for probate. The husband then remarried. Subsequently, he executed a new will and made a number of estate planning provisions in favor of his second wife that were inconsistent with the terms of the joint will. The husband died in 1981, and the various interested parties entered into an agreement of ownership that basically followed the terms of the joint will. The IRS concluded that the entire value of the ranch was includible in the husband's gross estate for federal estate tax purposes under I.R.C. §§ 2036 and 2041.

The IRS characterized the joint will arrangement as follows: in 1965, the decedent transferred a remainder interest in his community property share of the ranch for less than full and adequate consideration in money or money's worth, while retaining a life estate in, and a power of appointment over, that share of the ranch sufficient to cause inclusion of the value of the interest in his gross estate under I.R.C. § 2036(a). In addition, he received a general power of appointment (by virtue of the power to mortgage the property and to execute and convey mineral leases on the ranch) over his first wife's community property share of the ranch sufficient to cause inclusion of the value of that interest in his gross estate under I.R.C. § 2041.

The letter ruling did not address the application of I.R.C. § 2043(a), discussed in section 9.72, *infra*, which provides for a reduction in the amount includible in the survivor's estate by the value of consideration received for the transfer. If, in fact, the husband received what was tantamount to fee ownership of the first wife's community property interest in the ranch by virtue of powers that the IRS characterized as a general power of appointment over that share, it could be argued that the consideration was equal to, or exceeded, the interest that he gave up with respect to his community property interest. In any event, the first wife's former community property share of the ranch was included in the husband's estate under I.R.C. § 2041, while his former community



property share was included under I.R.C. § 2036(a) as a transfer with a retained life interest.

#### **4. Specific Problems Involving Gifts in Trust** **[§ 9.64]**

The basic principles concerning retained life interests discussed in the preceding sections are generally relevant to transfers in trust that are, or that become, irrevocable. The following example illustrates this.

➤ **Example 1.** A husband transfers marital property assets over which he has exclusive management and control into a revocable trust. The trust directs the trustee to pay income to the wife during her lifetime, grants the trustee the authority to make discretionary distributions of principal among the wife and their children during the wife's life, and gives a remainder interest to their children at her death. The husband reserves the power to revoke during his lifetime. The husband dies. The wife does not seek to recover her one-half marital property interest from the trust after the husband's death.

The wife's failure to recover her one-half marital property interest from the trust after the husband's death is likely to be regarded a completed gift of a remainder interest to the children not later than when the right to recover lapses. *See supra* §§ 2.102, 4.36, *infra* § 9.91. When the wife subsequently dies, one-half of the value of the trust assets will be includible in her estate under I.R.C. § 2036(a) as a transfer with a retained life estate. Even if the wife dies before expiration of her right to recover one-half of the marital property assets in the trust, it is probable that one-half of the value of the trust at the wife's death will be includible in her estate under I.R.C. § 2038 as a transfer subject to a power to revoke. *See infra* § 9.65.

The problem in the above example may be particularly acute if the husband believes that he is funding the trust with non-marital property assets, but in fact there is a marital property component. By the time this is discovered after the husband's death, the wife may be deemed to have made a completed gift of the remainder interest in her half of the marital property assets; in addition, she may be deemed to have retained an income interest for life, which will subject her marital property share of the assets to federal estate taxes under I.R.C. § 2036(a).

The retained interest rule of I.R.C. § 2036 also has potential hazards for irrevocable life insurance trusts, as illustrated by the following example.

➤ **Example 2.** A wife creates an irrevocable life insurance trust and assigns to it a number of annually renewable employment-related group term life insurance policies on her life. Income from the trust is payable to her husband during his lifetime, and the remainder interest is given to the couple's children. The wife's employer pays the policy premiums each year as an incident of employment. No marital property agreement under section 766.58 or life insurance consent under section 766.61(3)(e) is executed in an effort to reclassify the premium payments as the individual property of the insured wife. After the payment by the employer of a number of premiums, the wife dies.

Based on these facts, the entire amount of the insurance proceeds payable to the trustee might be characterized as marital property because the premium for the annually renewable policy is paid with marital property funds. If the husband does not seek to withdraw from the trust his one-half marital property interest in the insurance proceeds under section 766.70(6)(b) following the wife's death, a completed gift might be deemed to have taken place to the children, who receive the remainder interest in such one-half of the insurance proceeds. *See United States v. Gordon*, 406 F.2d 332 (5th Cir. 1969) (applying Texas law); *Whiteley v. United States*, 214 F. Supp. 489 (W.D. Wash. 1963). This will constitute a transfer with a retained life estate under I.R.C. § 2036(a), and one-half of the value of the insurance trust will be includible in the husband's estate at his death, contrary to the tax planning objectives of the spouses.

### **G. Federal Estate Tax: Powers to Revoke and Powers of Appointment [§ 9.65]**

Several cases have raised questions concerning the existence of a general power of appointment when one or both spouses transferred community property into a revocable trust. The most detailed and interesting of these decisions is *Katz v. United States*, 382 F.2d 723 (9th Cir. 1967), which involved principles of California community property law similar to those that apply in Wisconsin under the Act. *See Wis. Stat. § 766.31(5)*.

In *Katz*, the husband created a trust of community property with an independent trustee. The trust declaration reserved the income to the husband for life, provided the wife with income for life thereafter, and finally distributed income and principal to his children and the issue of his children. The husband alone reserved the power to revoke the entire trust. The wife signed a written approval of the trust. The IRS sought to include the entire value of the trust in the husband's estate on the theory that either the wife's approval of the trust arrangement accomplished a transmutation of the community property into the husband's separate property, or, alternatively, that the husband possessed a general power of appointment over the wife's one-half of the trust assets that was taxable under I.R.C. § 2041, as well as possessing an I.R.C. § 2038 power to revoke with respect to his own one-half of the trust assets.

The court held that only the husband's one-half community property interest in the trust assets was includible in his estate under I.R.C. § 2036 or I.R.C. § 2038. Despite the husband's general management and control powers over the community property under California law, he could not make a gift of this property to himself or others without the express consent of the wife. The wife's approval of the trust did not constitute consent and, at best, constituted a transfer to the trustee of her one-half interest in the community property. Accordingly, the husband acted only as an agent for the community in funding the trust. The property transferred to the trust remained community property and was not transmuted to the separate property of the husband.

The court also rejected the argument that the husband held a general power of appointment over the wife's one-half community property interest in the trust, noting that the husband's powers over the trust were either managerial in nature or a power to revoke the trust, acting as agent for the community. The court reasoned that these powers were no more than the powers of management and control that the husband otherwise had over the community property before the transfer to the trust, and did not constitute a general power of appointment under I.R.C. § 2041.

These facts should produce the same result under the Act. Under Wisconsin law, the transfer of marital property assets into a revocable trust does not, by itself, change the classification of the assets. Wis. Stat. § 766.31(5). The comment to section 4 of the Uniform Marital Property Act (UMPA), *reprinted infra* app. A, makes clear that the principal enabling function of this subsection "is to permit the creation of revocable living trusts by one or both spouses without any automatic

reclassification of property committed to the trust.” The managerial rights over the trust retained during lifetime by the husband would not destroy the marital property nature of the trust assets. Wis. Stat. § 766.51(5). No completed gift to third parties could occur before the death of the husband, because of the power to revoke. At the husband’s death, both the husband’s and the wife’s respective halves of the marital property assets would pass in accordance with the terms of the trust. The gift of the husband’s interests would be complete at that time. If the surviving wife failed to assert her right to recover her half of the marital property assets under section 766.70(6)(a) or (b) (or other applicable provisions) within the appropriate time limit, a completed gift of the remainder interest in her half would be made to third parties. *See supra* § 9.64, *infra* § 9.91.

If the wife died before the expiration of the limitation period for recovery of her one-half interest in the marital property assets in the trust, it is likely that one-half of the value of the trust assets would be includible in her estate under I.R.C. § 2033 as a claim or cause of action, or under I.R.C. § 2038 as a transfer subject to a power of revocation. *See, e.g., Estate of Lucey v. Commissioner*, 13 T.C. 1010 (1949). Similarly, if the wife predeceased the husband, her personal representative clearly would have the right to recover her one-half interest in the marital property assets held in the revocable trust. *See* Wis. Stat. § 766.31(5); *see also supra* § 2.102. This one-half interest would be included in her estate under I.R.C. § 2033. *See supra* § 9.58.

Results similar to those in *Katz* have occurred in the few cases that have considered the question of a general power of appointment. *See Albuquerque Nat’l Bank v. United States*, 80-1 U.S.T.C. (CCH) ¶ 13,329 (10th Cir. 1979) (holding that wife’s power to amend or revoke trust was limited to half of the trust estate after husband’s death and thus did not constitute a general power of appointment over the other half); *Tucker v. United States*, 74-2 U.S.T.C. (CCH) ¶ 13,026 (S.D. Cal. 1974) (holding that husband and wife’s power of revocation was joint during their lifetimes and could not be exercised by wife after husband’s death; hence, she had no general power of appointment). It would follow from *Tucker* that if a revocable trust is created with marital property assets, and if the trust instrument reserves the power to revoke the entire trust to either or both spouses during their joint lifetimes or to the survivor thereafter, the survivor will possess a general power of appointment under I.R.C. § 2041 with respect to the deceased spouse’s former one-half of the marital property assets in the trust, and in addition will retain

an I.R.C. § 2038 power to revoke with respect to his or her own one-half. *See, e.g.*, Tech. Adv. Mem. 9431004 (Aug. 5, 1994) (joint will in which surviving spouse effectively possessed a general power of appointment over both spouses' halves of community property assets subject to the will).

## **H. Federal Estate Tax: Retirement Benefits [§ 9.66]**

### **1. ERISA Preemption [§ 9.67]**

Wisconsin has adopted a terminal-interest rule providing that the marital property interest of a nonemployee spouse in the deferred-employment-benefit plans of the employee spouse terminates at death if the nonemployee spouse predeceases the employee spouse. Wis. Stat. §§ 766.31(3), .62(5). This terminal-interest rule also applies to the marital property interest of the nonemployee spouse in IRA assets that are traceable to the rollover of a deferred-employment-benefit plan, meaning that the nonemployee spouse's interest in such rollover IRA will terminate if he or she predeceases the employee spouse. *Id.* Accordingly, pursuant to the terminal-interest rule, no marital property interest remains in the deceased nonemployee spouse that is includible in his or her gross estate.

In those community property jurisdictions that, unlike Wisconsin, have not adopted a terminal-interest rule for the nonemployee spouse's interest in deferred employment benefits, the question of whether one-half of an employee spouse's deferred employment benefits should be included in the estate of a deceased nonemployee spouse had historically proven to be a major area of uncertainty, especially if the benefits were subject to disposition to third parties by the nonemployee spouse's will or through intestacy. Such uncertainty was put to rest, however, by the Supreme Court's decision in *Boggs v. Boggs*, 520 U.S. 833 (1997), in which the Court held that ERISA preempts state community property laws that grant a deceased nonemployee spouse property rights in an employee spouse's qualified deferred employment benefits.

Under the terms of the Retirement Equity Act of 1984 (REA), Pub. L. No. 98-397, 98 Stat. 1426, amending various provisions of the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. §§ 1001–1461, nonemployee spouses were granted extensive rights with respect to benefits under qualified retirement plans subject to regulation under

federal law. Generally speaking, these rights cannot be defeated by the employee spouse unless the nonemployee spouse gives an express written consent executed in compliance with I.R.C. § 417(a)(2)(A). Because the REA vests such extensive rights in the nonemployee spouse with respect to qualified plan benefits, there was some question before *Boggs* whether such a spousal consent to the release of those rights and to the designation of third-party beneficiaries by the employee spouse might have adverse federal estate and gift tax consequences with respect to any community property interest that the nonemployee spouse might have in such benefits under state law. It is now clear, however, after the Supreme Court's decision in *Boggs*, that ERISA preempts state community property laws and that the nonemployee spouse should be able to give such consent with no adverse transfer tax consequences.

*Ablamis v. Roper*, 937 F.2d 1450 (9th Cir. 1991), was the first federal decision to consider the issue of federal preemption under ERISA of the nonemployee spouse's community property rights in the employee spouse's qualified retirement plan benefits upon the death of one of the spouses. The question posed in *Ablamis* was whether the will of a predeceasing nonemployee spouse, which purported to dispose of all of her community property interests in trust for the benefit of her children from a prior marriage, reached her community property interest in her surviving husband's retirement plan. The court held that (1) the purported transfer by the nonemployee spouse of her one-half community property interest in the retirement benefits was subject to the anti-assignment provision in ERISA, 29 U.S.C. § 1056; (2) any probate court order directing a transfer of a portion of the plan benefits would not be a QDRO made pursuant to a state's domestic relations law, and thus would not qualify for the QDRO exception to the anti-assignment provision; and (3) to the extent that California law permitted testamentary transfer of a deceased nonemployee spouse's community property interest in the employee spouse's retirement benefits, it was preempted by ERISA. *Ablamis* was followed in *Meek v. Tullis*, 791 F. Supp. 154 (W.D. La. 1992), in which the court held that ERISA preempted Louisiana community property laws that otherwise might be applicable to intestate succession of an interest in a qualified pension plan. These cases supported the position, later confirmed by the Supreme Court in *Boggs*, that except as allowed by the limited QDRO exception, state community property laws are ineffective to divest a participant of his or her interest in a qualified plan governed by ERISA.

*Boggs* was also a Louisiana case, but this time the district court reached a contrary result, holding that ERISA did not preempt Louisiana community property laws to defeat the community property interest in qualified plan benefits that accrued to a predeceased nonemployee spouse. *Boggs v. Boggs*, 849 F. Supp. 462 (E.D. La. 1994). The decedent had married his first wife in 1949. She died in 1979, and he remarried in 1980. At all times up to his retirement in 1985, he was employed by the same company. Following his death in 1986, his surviving second wife brought suit against his sons by his first marriage to determine whether, under ERISA, his designation of her (the surviving spouse) as beneficiary of various qualified retirement plan benefits cut off the sons' former community property rights in the plan benefits they had inherited through their mother.

The district court concluded that “despite its broad preemption provision, ERISA does not preempt state laws such as Louisiana’s community property laws which were not specifically designed to affect ERISA benefit plans.” The court reasoned that while state community property laws might indirectly implicate an ERISA plan, they do not “relate to” such plans in the manner required to trigger preemption. The court went on to state that ERISA will preempt Louisiana’s community property law if and only if (1) Congress has positively expressed its intent to preempt the state law, and (2) the state law does major damage to a clear and substantial federal interest.

After analyzing a number of Supreme Court precedents, the court concluded that the application of state community property laws does not do major damage to substantial federal interests. The court noted that a finding that ERISA preempts state community property laws would provide a strong incentive for a nonemployee spouse in a community property state to obtain a divorce before death as the only method of retaining transmissible property rights in the employee spouse’s qualified retirement plan benefits. Further, the court noted that permitting the spousal benefit rights under ERISA to override a prior spouse’s vested community property interest would violate the Fifth Amendment’s prohibition against governmental takings of private property without just compensation. The court also made reference to *Hisquierdo v. Hisquierdo*, 439 U.S. 572 (1979), in which the Supreme Court instructed that there is a presumption against preemption in areas of traditional state regulation such as family law.

The Fifth Circuit Court of Appeals affirmed the district court's decision and the Supreme Court granted certiorari because of the conflict between the Fifth Circuit in *Boggs* and the Ninth Circuit in *Ablamis*. *Boggs*, 520 U.S. 833. The Court first noted that the case was important in that it affected 80 million residents of community property states with more than \$1 trillion in qualified plan benefits. After announcing that its decision would also affect claims in common law jurisdictions, the Court announced a very broad ERISA preemption test:

ERISA's express preemption clause states that the Act "shall supersede any and all state laws insofar as they may now or hereafter relate to any employee benefit plan...." We can begin, and in this case end, the analysis simply by asking if state law conflicts with the provisions of ERISA or operates to frustrate its objects. We hold that there is a conflict, which suffices to resolve the case. We need not inquire whether the statutory phrase "relate to" provides further and additional support for the pre-emption claim.

*Id.* at 841 (citation omitted).

Accordingly, the bottom line of the Court's holding in *Boggs* is that it is necessary for community property laws to yield to ERISA when such laws affect a field that Congress has appropriated for a federal purpose to carry out a uniform federal scheme. In determining whether Congress intended to preempt community property laws, the Court examined several provisions of ERISA and determined that the purpose of the law is to protect the interests of participants and beneficiaries. The Court then examined QDROS and the rules requiring joint spousal annuities that the REA provides for a nonparticipant spouse and declared the following:

The surviving spouse annuity and QDRO provisions, which acknowledge and protect specific pension plan community property interests, give rise to the strong implication that other community property claims are not consistent with the statutory scheme. ERISA's silence with respect to the rights of a nonparticipant spouse to control pension plan benefits by testamentary transfer provides powerful support for the conclusion that the right does not exist.

*Id.* at 847–48.

The Court further stated that ERISA's anti-alienation provisions give "specific and powerful reinforcement" to the preemption argument and went on to find that the participant's sons from his first marriage were



neither participants nor beneficiaries in their father's pension plan. Based on its premise that ERISA was designed to protect beneficiaries and participants, the Court reasoned that under Louisiana law, community property interests are enforceable against a qualified plan, and that if the sons' claims were allowed to succeed, they would have acquired an interest in their father's pension plan at the expense of plan participants and beneficiaries. The Court concluded that such a result would be contrary to the purposes of ERISA and dictated that preemption should apply.

The Court finally noted that whether the interest of the sons was enforced against their father's pension plan or against his surviving spouse (the recipient of the benefits), the result was the same. Stressing again the need to protect beneficiaries and participants, the Court instructed that "ERISA is for the living" and in summary, advised:

It does not matter that respondents have sought to enforce their right only after the retirement benefits have been distributed since their asserted rights are based on the theory that they had an interest in the undistributed pension plan benefits. Their state-law claims are pre-empted.

*Id.* at 854.

In *Egelhoff v. Egelhoff*, 532 U.S. 141 (2001), the Supreme Court reiterated the strong stance it took in *Boggs* that ERISA preemption can apply to override state statutes, even in areas of traditional state regulation such as family law and probate law. The case involved a divorced decedent in Washington state whose benefits from his employer included a life insurance policy and a pension plan both governed by ERISA. Before his divorce, the decedent had designated his ex-wife as the beneficiary of these benefits, which he received as part of the division of community property in the divorce. The decedent died in an automobile accident two months after the divorce, having never removed his ex-wife as beneficiary of the plan benefits. His children from another previous marriage subsequently brought an action against the ex-wife to recover the benefits based on section 11.07.010(2)(a) of the Washington Revised Code, which then stated as follows:

If a marriage is dissolved or invalidated, a provision made prior to that event that relates to the payment or transfer at death of the decedent's interest in a nonprobate asset in favor of or granting an interest or power to the decedent's former spouse is revoked. A provision affected by this section must be interpreted, and the nonprobate asset affected passes as if the former

spouse failed to survive the decedent, having died at the time of entry of the decree of dissolution or declaration of invalidity.

The ex-wife defended the action by claiming that the statute could not operate to deny her the benefits because it was preempted by ERISA. The trial court ruled in favor of the ex-wife, but the Washington Supreme Court overruled and held in favor of the children. The U.S. Supreme Court granted certiorari, stating that it agreed to review the case because courts have disagreed whether statutes like that of Washington are preempted by ERISA.

The Court ruled in favor of the ex-wife, holding that ERISA preempted the children's claims. The Court reasoned that the Washington statute directly conflicts with ERISA, because the result of applying the state law is that plan administrators must pay benefits in accordance with state law, rather than in accordance with plan documents. Thus, the Court stated the Washington statute interferes with the goal of nationally uniform ERISA plan administration.

The Court went on to state that while there is indeed a presumption against federal preemption in areas of traditional state regulation such as family law, that presumption can be overcome in situations in which Congress has made clear its desire for preemption. Referring to *Boggs*, the Court noted that it had previously not hesitated to find state family law preempted when it conflicts with ERISA or relates to ERISA plans. The Court further reasoned that ERISA preemption over state law was necessitated in such situations because requiring ERISA administrators to master the relevant laws of all 50 states would undermine the congressional goal of minimizing the administrative and financial burdens on plan administrators.

Based on *Boggs* and *Egelhoff*, it appears well settled that ERISA will preempt state community property laws and other state-specific statutes that would hinder uniform qualified-plan administration. Therefore, a nonemployee spouse residing in a community property state will have no legal interest in an employee spouse's qualified retirement plan other than those provided for under the REA, and the assets inside the qualified plan will not be subject to state community property laws. Moreover, because preemption applies, this result cannot be modified by spouses in a marital property agreement to provide for an interest in the plan for the nonemployee spouse.

## 2. IRAs [§ 9.68]

When analyzing possible estate tax planning strategies for married couples, it should be kept in mind that IRAs and individual retirement annuities (considered IRAs for purposes of this discussion) are expressly not subject to ERISA preemption. Instead, the ownership of an IRA is governed by state law, including community property law.

It seems likely that IRAs (even rollover IRAs funded with proceeds from qualified plans) do not fall under the *Boggs* preemption decision and thus can be structured to include a community property ownership interest in the nonparticipant spouse. Support for this position can be found in the *Boggs* decision itself, in which Justice Kennedy, writing for the majority, specifically stated:

[T]his case does not present the question whether ERISA would permit a non-participant spouse to obtain a devisable community property interest in benefits paid out during the existence of the community between the participant and that spouse.

*Boggs*, 520 U.S. at 845.

The argument that state community property laws control rollover IRAs and that federal preemption does not apply is also supported by the fact that recognizing community property ownership of IRAs does not make compliance with federal ERISA regulations unnecessarily burdensome on plan administrators, because IRAs are not even subject to ERISA. Therefore, many community property experts believe that as soon as qualified plan benefits are rolled over into an IRA, state community property laws control the ownership rights of the spouses.

Ownership of an IRA as community property can potentially provide favorable estate tax planning options for married couples, especially if one spouse owns a large IRA and the other spouse does not have sufficient assets to fully utilize his or her personal estate tax exemption. If the spouses can own the IRA in equal shares as community property, the estate tax equalization problem can often times be solved.

➤ **Note.** For a comprehensive discussion of planning for IRAs in community property jurisdictions, see Edward V. Brennan, *Planning for Community Property Retirement Benefits and IRAs*, Estate Planning, Apr. 2002, at 187.

Historically, there has been no consistent or clear authority as to whether federal tax law will recognize all or a portion of an IRA as community property. *See, e.g.*, I.R.C. § 408(g) (community property laws are to be disregarded for purposes of applying the IRA provisions of the Code); *Bunney v. Commissioner*, 114 T.C. 259 (2000); *Morris v. Commissioner*, 83 T.C.M. (CCH) 1104 (2002) (holding that state community property laws will not apply to IRA distributions, which are instead taxable solely to the IRA owner and reported only on his or her separate tax return). But in a series of recent private letter rulings, the IRS has clarified that I.R.C. § 408(g) does not affect actual property rights, which are to be governed by applicable state law and that the determination whether an IRA should be classified as community property lies outside the scope of I.R.C. § 408. *See* Priv. Ltr. Rul. 200928043 (Apr. 14, 2009); Priv. Ltr. Rul. 200935045 (June 1, 2009); Priv. Ltr. Rul. 200950053 (Sept. 18, 2009) (construing I.R.C. § 408(g) to allow basic recognition of community property rights of the spouse of an IRA owner with varying rulings on income tax consequences of such classification). For older similar rulings from the IRS, see Private Letter Ruling 199937055 (Sept. 17, 1999), Private Letter Ruling 9439020 (Sept. 30, 1994), and Private Letter Ruling 8040101 (July 15, 1980).

It is important to note that the statutory terminal-interest rule in section 766.31(3) specifically applies to assets in an IRA that are traceable to the rollover of a deferred-employment-benefit plan. Therefore, absent a provision in a marital property agreement to the contrary, the interest of the nonemployee spouse in such a rollover IRA terminates if he or she predeceases the employee spouse. Accordingly, if a Wisconsin married couple wants to take advantage of the planning possibilities that may be available if a rollover IRA is classified as marital property, the couple should specifically negate the application of section 766.31(3) to the IRA in a marital property agreement.

## **I. Federal Estate Tax: Proceeds on Life Insurance and Interest in Life Insurance Contracts [§ 9.69]**

### **1. Individually Owned Contracts [§ 9.70]**

The proper federal estate tax treatment of life insurance proceeds received upon the death of the insured may come into question when the insurance policy was formerly community property and the insured did

not own all the interests in the contract at the time of the noninsured spouse's death. Ordinarily, this issue is presented only when the spouses have a marital property agreement that eliminates the *frozen-interest* rule of section 766.61(7) (i.e., an agreement that provides that the noninsured spouse's interest in the policy on the insured spouse's life will not terminate if the noninsured spouse predeceases the insured spouse). *See supra* § 2.178. This situation is reflected in the following example from Treasury Regulation § 20.2042-1(c)(5), which confirms that an insured spouse holds incidents of ownership in a policy requiring estate inclusion under I.R.C. § 2042 only to the extent that the insured spouse is treated as owning an interest in the policy under the local community property law:

As an additional step in determining whether or not a decedent possessed any incidents of ownership in a policy or any part of a policy, regard must be given to the effect of the state or applicable law upon the terms of the policy. For example, assume that the decedent purchased a policy of insurance on his life with funds held by him and his surviving wife as community property, designating their son as beneficiary but retaining the right to surrender the policy. Under the local law, the proceeds upon surrender would have inured to the marital community. Assuming that the policy was not surrendered and that the son receives the proceeds on the decedent's death, the wife's transfer of her one-half interest in the policy is not considered absolute before the decedent's death. Upon the wife's prior death, one-half of the value of the policy would have been included in her gross estate. Under these circumstances, the power of surrender possessed by the decedent as agent for his wife with respect to one-half of the policy is not, for purposes of this section, an "incident of ownership," and the decedent, therefore, is deemed to possess an incident of ownership in only one-half of the policy.

This rule was applied by the Tax Court in *Estate of Burris v. Commissioner*, 82 T.C.M. (CCH) 400 (2001). In this case, Burris and his wife lived in Louisiana (a community property state) and, while married, he purchased three policies on his life naming himself as owner and paying the premiums using community property funds. The couple did not have a marital property agreement, and there was no evidence presented that they did not intend to hold the policies as community property. Burris's wife predeceased him and one-half of the cash values of the policies was reported in her estate (unlike Wisconsin, Louisiana apparently does not have a frozen-interest rule, which would have terminated the wife's interest at Burris's death absent an agreement to the contrary). Burris died less than a year later, with the couple's

children receiving the policy proceeds. His personal representative treated the policies as community property and reported only one-half of the proceeds in his estate.

The Tax Court agreed with the position taken by Burris's estate and held that under Louisiana law, the life insurance policies were community property. The court accordingly held that because Burris owned only a one-half interest in the policies (with his wife's estate owning the other half), only one-half of the proceeds were includible in his estate under I.R.C. § 2042.

In Action on Decision 2003-17, I.R.B. 811, the IRS acquiesced in result only to the Tax Court's decision in *Estate of Burris*. It subsequently issued Revenue Ruling 2003-40 on substantially the same facts as *Estate of Burris*, reaching the same conclusion as the Tax Court. It cautioned, however, that taxpayers will be held to a duty of consistency in reporting the estate tax treatment of community property life insurance in the estates of the husband and wife. For example, the IRS warned that a community property policy owned by a husband and insuring his life might be required to be included 100% in his estate if his wife predeceases him and her one-half share of the value of the policy is not included in her estate.

In *Scott v. Commissioner*, 374 F.2d 154 (9th Cir. 1967), involving California law, the noninsured wife predeceased her husband, leaving the residue of her estate (including her community property interest in insurance policies on her husband's life) to her sons. After the wife's death, the insured husband made additional premium payments on the policies from his separate funds. After a careful review of California cases, the court concluded that when the noninsured wife died and bequeathed her one-half community interest in the policies to her sons, the sons became tenants in common of the policies with the insured husband. When the insured husband subsequently paid additional premiums on the policies with separate funds, he acquired an additional interest of his own. The interest that he and the sons held in the policies as tenants in common was thereby diminished. The net result was that the ultimate fraction of the policy proceeds included in the insured husband's estate at his death was greater than one-half. Note that the court might have resolved the case by holding that the co-ownership shares of the husband and the sons in the policy and the proceeds did not change as a result of the subsequent premium payments by the husband, and that the husband merely had a right to reimbursement from the sons

for half of the premium payments he advanced following the wife's death.

The question of including life insurance proceeds in the estate of the second spouse to die was also the primary issue in *Estate of Cavanaugh v. Commissioner*, 51 F.3d 597 (5th Cir. 1995) *rev'g* 100 T.C. 407 (1993). The decedent and his wife were residents of Texas. In 1980, they purchased a term life insurance policy on the decedent's life. The policy had a one-year term and could be renewed automatically by making annual payments of increasing premiums. The policy had no cash value or loan value but provided an annual dividend. The decedent renewed the policy each year until his death, both before and after the death of his wife, who predeceased him by three years.

The proceeds of the policy were paid to the decedent's estate as beneficiary. The personal representative of the decedent's estate included only one-half of the policy proceeds in his gross estate, arguing that, under Texas community property law, the estate had no more than a one-half interest in the policy and its proceeds. The personal representative further contended that the other one-half interest had passed through the estate of the decedent's late wife into the residuary trust under her will, and that this trust was entitled to the other one-half of the policy and the proceeds.

The IRS took the position that the entire death benefit was includible in the decedent's estate. The Tax Court agreed with the IRS, noting that under Texas community property law the general rule is that the community interest of an uninsured spouse who predeceases the insured spouse is settled by distributing an amount equal to one-half of the cash surrender value of the unmatured policy to the uninsured spouse's estate and the other one-half interest (plus ownership of the unmatured policy) to the insured spouse. (This property law rule is somewhat similar to the terminal-interest rule found in section 766.61(7)). In the case of a term insurance policy having no cash surrender value (as here), Texas uses the interpolated-terminal-reserve method of valuation to determine the uninsured spouse's community property interest in the policy. Because the record in this case did not establish that the policy had any cash surrender or terminal-reserve value on the date of the wife's death, her community property interest in the policy was worth nothing, and no distribution to her estate was necessary to settle her community interest in the policy. Accordingly, her estate had no rights in the policy or its proceeds on the date of her death, and the policy devolved entirely to the

decedent. As a result, the decedent's gross estate included the entire death benefit payable under the policy.

The Fifth Circuit reversed the Tax Court's decision, relying on the strained reasoning that the wife's estate still retained a one-half interest in the policy because her property had not yet been settled or partitioned in the three years after her death and before the decedent's death. The court stated that according to Texas law, under circumstances in which the uninsured spouse predeceases the insured spouse, settlement of the decedent's community property interest (in the policy) has ordinarily been resolved by allocating one-half of the cash surrender value to the deceased spouse's estate and the other half to the surviving spouse. In this case, however, the court reasoned that the wife's property was not settled or partitioned before the decedent's death so that her one-half community property interest in the policy was never extinguished and remained intact up to the date of the decedent's death. Accordingly, the court ruling appears very fact-specific and perhaps overreaching in its attempt to include only one-half of the proceeds in the decedent's estate.

*Estate of Cervin v. Commissioner*, 111 F.3d 1252 (5th Cir. 1997), *rev'g* 68 T.C.M. (CCH) 1115 (1994), also involving Texas law, dealt with life insurance policies possessing cash-surrender value in a similar factual context. In this case, the Tax Court concluded that the predeceasing noninsured wife's community property interest in the policies was settled before the decedent's death, because one-half of the cash surrender value had been allocated to her estate and reported on her federal estate tax return. Further, because the couple's children (who were beneficiaries of her estate) failed to assert their right to compensation from the policies equivalent to their mother's community interest during the 10-year interval between her death and the death of the insured spouse, the children's interest in the policies was effectively abandoned. Accordingly, the children were not entitled to one-half of the cash surrender value of the policies at the insured's death, and the entire proceeds of the policies were includible in the insured's estate.

The Fifth Circuit again reversed the Tax Court, this time finding that although the wife's estate tax return listed her one-half interest in the cash value of the policy on her estate tax return, her interest in the policy was never settled during the 10-year period leading up to the death of the insured spouse because her children agreed with their father not to seek allocation of their share of the cash value but instead to keep the policy in place. Accordingly, the court concluded that because one-half of the



cash value was never distributed to the children, the deceased wife's interest in the insurance policies remained unsettled until her husband's death.

Although the Fifth Circuit reversed, a result similar to the Tax Court's decisions in *Estate of Cavanaugh* and *Estate of Cervin* likely would follow in Wisconsin, because the interest of the deceased noninsured spouse is a fixed and vested amount under section 766.07(7) and is not dependent upon an actual claim of payment by such spouse's successors-in-interest. Under section 766.70(7), a failure by the surviving insured spouse to purchase the marital property frozen interest of the deceased noninsured spouse would result in the passage of that interest to the beneficiaries of the noninsured spouse's estate. The failure of those beneficiaries to assert their ownership rights or pay a pro rata share of premiums might result in loss of those rights.

The question of the proper transfer-tax treatment of the proceeds of a life insurance policy on the life of a deceased spouse that was owned entirely by the surviving spouse, even though purchased with community funds, was addressed in Revenue Ruling 94-69, 1994-2 C.B. 241. Louisiana law was applicable to the facts. Pursuant to long-standing Louisiana statutory and common law, the presumption that property in the possession of either spouse during a marriage is community property does not apply to a life insurance policy transferred by or between spouses and specifically does not apply to life insurance that has been purchased with community funds and designates one spouse alone as the owner. Under these circumstances, policies on the life of one spouse that are unconditionally owned by the other spouse are, as a matter of law, deemed to be part of the owning spouse's separate estate. Accordingly, the proceeds are not includible in the deceased insured spouse's gross estate under I.R.C. § 2042.

Although the revenue ruling is based on and refers to Louisiana law, the principle involved also should apply to Wisconsin decedents. Like the comparable Louisiana statutory provision, section 766.61(3)(c)1, provides that the ownership interest in proceeds of a policy that designates the insured's spouse as the owner are the individual property of its owner, regardless of the classification of property used to pay premiums on the policy. If the principles of Revenue Ruling 94-69 are applied in Wisconsin—as they should be—the insured spouse's gross estate will not include the proceeds of a policy on his or her life that was owned by his or her spouse.

➤ **Note.** If a person other than the owner-spouse is named as beneficiary, Revenue Ruling 94-69 takes the position that on the death of the insured, a completed gift of the total amount of the proceeds will be deemed to have taken place from the surviving owner spouse to the beneficiary. *See also* Treas. Reg. § 25.2511-1(h)(9) (if property held by husband and wife as community property is used to purchase insurance on husband's life and third party is named beneficiary, on husband's death there is a gift by wife of one-half of amount of proceeds representing her one-half interest in policy).

## 2. Corporate-owned Contracts [§ 9.71]

As a general rule, if the insured owns a majority interest in the voting stock of a corporation, the incidents of ownership possessed by the controlled corporation over any policy on the insured shareholder's life will be attributable to the shareholder, except for proceeds of a policy payable directly to the corporation or payable to a third party for a valid business purpose. *See* Treas. Reg. §§ 20.2042-1(c)(6), .2031-2(f). This rule raises potential concerns when applied to majority stock interests owned by a husband and wife as community property. The IRS has privately ruled that stock separately owned by spouses that individually constitutes less than 50% of the corporation's combined voting power, but together exceeds 50% of the combined voting power, will not be aggregated under Treasury Regulation § 20.2042-1(c)(5). Priv. Ltr. Rul. 9808024 (Feb. 20, 1998) (spouses owned 72% of corporation's stock as community property); Priv. Ltr. Rul. 9037012 (Sept. 14, 1990) (spouses together owned 51.78% of corporation's stock).

Pursuing this line of reasoning could lead to the conclusion that if all (or any lesser amount) of the voting stock in a corporation is community property, there can never be a controlling stockholder, because neither spouse would ever own more than 50% of the stock. *See* Treas. Reg. § 20.2042-1(c)(5). This result is supported by the approach taken in valuation cases involving community property. *See supra* § 9.56. Yet in cases in which the community property stock is held in the name of only one spouse who alone exercises exclusive management and control over the stock, including voting rights, that spouse might be deemed to be a controlling shareholder for purposes of the regulation. It is much more likely that the rationale of the IRS's private letter rulings on this issue will be applied if the stock is held in the names of both spouses (since

joint management and control would be required), or if one half of the community property stock is registered in each spouse's name. Of course, the possible estate tax benefits that dual holdings of stock may have with respect to corporate-owned life insurance may necessarily have to yield to practical business considerations that favor having one spouse alone hold the stock in the corporation.

## **J. Federal Estate Tax: Transfers for Insufficient Consideration [§ 9.72]**

### **1. Forced-election Estate Plans [§ 9.73]**

The typical estate tax result of a surviving spouse's surrender of his or her one-half interest in community property for inadequate consideration under a forced-election estate plan is that, because of the survivor's retention of a life-income interest in it, the one-half interest will later be included in the surviving spouse's estate under I.R.C. § 2036(a). The half interest recaptured at the date of the survivor's death is valued in full as of that date. However, some mitigation of the estate tax consequences is provided by I.R.C. § 2043(a), which allows for a reduction of the amount includible in the survivor's estate. If a transfer, trust, interest, right, or power described in I.R.C. §§ 2035 to 2038 or 2041 is made, created, exercised, or relinquished for a consideration in money or money's worth, but is not a bona fide sale for adequate and full consideration in money or money's worth, the amount included in the surviving spouse's gross estate is the *excess* of the fair market value of the surviving spouse's one-half interest in former community property contributed to the deceased spouse's trust, *valued at the time of the survivor's death*, over the value of the consideration received for the transfer by the (now deceased) surviving spouse. I.R.C. § 2043(a). The value of the consideration received is the present value of the income interest received by the now deceased surviving spouse in the first deceased spouse's half of the community property, *valued at the time of the first spouse's death*. *Gradow*, 11 Cl. Ct. 808; *Estate of Gregory v. Commissioner*, 39 T.C. 1012 (1963); *Whiteley v. United States*, 214 F. Supp. 489 (W.D. Wash. 1963); *United States v. Gordon*, 406 F.2d 332 (5th Cir. 1969). Several cases have ruled that the time of valuing the consideration is the date of the final decree in the first spouse's estate, rather than the date of death, if the date of the final decree was the last date under state law when an election against the will was possible.

*Estate of Christ v. Commissioner*, 480 F.2d 171 (9th Cir. 1973); *Estate of Sparling v. Commissioner*, 60 T.C. 330 (1973), *rev'd and remanded*, 552 F.2d 1340 (9th Cir. 1977); *see also United States v. Past*, 347 F.2d 7 (9th Cir. 1965) (involving computation of the value of property subject to a retained life estate, and the valuable consideration offset, under a divorce property settlement agreement).

As discussed in section 9.63, *supra*, there has been a debate between the federal circuit courts of appeal over whether the consideration deemed to have been transferred by the surviving spouse in a forced-election plan should be measured by the value of his or her remainder interest in the community property transferred (because the surviving spouse retains a life income interest in that property in addition to receiving a life interest in the deceased spouse's half of the community property) or by the full, undiminished value of his or her one-half interest in the community property transferred. *Compare Estate of D' Ambrosio v. Commissioner*, 101 F.3d 309 (3rd Cir. 1996), *rev'g* 105 T.C. 252 (1995) (holding that consideration flowing from surviving spouse should be measured by actuarial value of remainder interest in community property transferred); *Gradow*, 11 Cl. Ct. 808, *aff'd*, 897 F.2d 516 (holding that consideration flowing from surviving spouse consists of his or her full one-half interest in community property transferred).

The result of this valuation question is critical, because I.R.C. § 2036(a) and I.R.C. § 2043 interact in such a way that if the "adequate and full consideration" exception of section 2036(a) does not apply, then the "time-of-election" valuation of the consideration received by the surviving spouse is matched against the "time-of-death" valuation of the property included in his or her estate for purposes of applying the offset under section 2043. Consequently, if the property to be included in the surviving spouse's gross estate increases in value after the election, the offset under I.R.C. § 2043 can dramatically lose its impact. Theoretically, even a one-dollar deficiency in the consideration received by the surviving spouse at the time of the election will cause inclusion of the community property in the survivor's estate, which, although transferred, will have increased in value far beyond the one-dollar difference.

## 2. Release of Certain Marital Rights [§ 9.74]

Under I.R.C. § 2043(b), the relinquishment or promised relinquishment of dower or curtesy, of a statutory estate created in lieu of dower or curtesy, or of other marital rights in the decedent's property or estate shall not be considered consideration "in money or money's worth" for federal estate tax law purposes. The intent of this provision is to preclude the relinquishment of essentially inchoate rights in exchange for a transfer of property at death in an effort to defeat the application of the federal estate tax. If the experience with California's quasi-community property statute is any guide, it is likely that promised relinquishment of the right to elect deferred marital property under section 861.02 will not be considered consideration in money or money's worth for other transfers of property at the death of a spouse. *Estate of Sbicca v. Commissioner*, 35 T.C. 96 (1960). For reasons that will be discussed in section 9.81, *infra*, however, the adoption of an unlimited estate tax marital deduction in I.R.C. § 2056 has greatly reduced, if not totally eliminated, concerns of this sort over most transfers between spouses.

The allowance of debts and claims as deductions against a deceased spouse's estate under I.R.C. § 2053(a)(3) is also conditional on these obligations being contracted for full and adequate consideration in money or money's worth. I.R.C. § 2053(c)(1). The rules of I.R.C. § 2043(b) concerning relinquishment of marital rights are made applicable to the debts and claims provisions of the Internal Revenue Code by I.R.C. § 2053(e).

In *Estate of Carli v. Commissioner*, 84 T.C. 649 (1985), the Tax Court held that the surrender by a wife of her community property rights in the earned income of her husband in exchange for the grant of a life estate in the husband's residence was adequate and full consideration for purposes of I.R.C. § 2043(b), thus permitting the deduction of the commuted value of the life estate as a claim against the deceased husband's estate under I.R.C. § 2053(a)(3). In *Estate of Herrmann v. Commissioner*, 85 F.3d 1032 (2d Cir. 1996), however, a deceased husband's estate was not allowed to deduct, as a claim against the estate, the value of a surviving wife's life estate in a residence that the decedent bequeathed to her pursuant to the terms of a prenuptial agreement in which the wife waived any right to an equitable distribution of the couple's property upon divorce.

The *Estate of Herrmann* court began by giving some insight on the tax-avoidance device its denial of the estate's claim was intended to prevent. The court instructed that I.R.C. § 2043(b)(1) is designed to prevent a married couple from entering into agreements that use consideration that is valid under state contract law to transform nondeductible marital rights—such as dower—into deductible contract claims against the estate, thereby depleting the taxable estate. The court went on to state that married couples normally will have no reason to structure bequests to each other as contractual debts, because most transfers between spouses should qualify for the estate tax marital deduction. The court noted, however, that life estates (and other terminal interests) for the benefit of a surviving spouse are not eligible for the marital deduction, because they end at the survivor's death and are not included in the survivor's taxable estate. Therefore, it follows that, absent I.R.C. § 2043(b), married couples would have a significant interest in the converting nondeductible life interests into deductible claims against the estate.

Stressing that the couple in *Estate of Herrmann* (who resided in New York, a common law state) remained married until the husband's death, the court then distinguished *Estate of Carli* by reasoning that the crucial fact in that case was that the widow's community property interest in her husband's future earnings was a presently enforceable right and that absent her waiver of that interest, half of his earnings would have been excludable from his gross estate because they would have been her property, not his. Therefore, because the widow's waiver increased her husband's taxable estate, any transaction in which she received equivalent value would not give rise to the tax avoidance I.R.C. § 2043(b) is intended to prevent.

By contrast, the court noted that the widow in *Estate of Herrmann* had no currently enforceable claim against any of her husband's property nor would she ever obtain such a claim during their marriage. At most, she traded away a contingent future right to an equitable share of her husband's property in the event of a divorce. Because no divorce took place and the couple was still married at the husband's death, the wife's waiver did not add anything to his estate. Therefore, the court reasoned that if it allowed the deduction for the wife's life estate, the effect would be that the husband's taxable estate would be diminished by the full amount of what he gave up in exchange for a waiver by his wife that added nothing to his estate. The court concluded that such a result is precisely what I.R.C. § 2043(b) was designed to prevent.

It is important to note that I.R.C. § 2043(b)(2) contains an exception for certain transfers under divorce-related property settlements that can be treated as having been made for an adequate and full consideration in money or money's worth. In order to qualify for this exception, the settlement must involve transfers of property or interests in property in satisfaction of marital or property rights under an arrangement that qualifies as nontaxable for gift tax purposes under I.R.C. § 2516(1). This is intended to permit deductibility of any unpaid portions of such arrangements as an indebtedness under I.R.C. § 2053(e).

Significantly, only the value of property transferred from one spouse to another spouse qualifies for the exception under I.R.C. § 2043(b)(2). This requirement was pointed out by the IRS in Technical Advice Memorandum 9527007 (July 7, 1995), in which spouses entered into an agreement in connection with their divorce under which the husband transferred property to an irrevocable trust that entitled the wife to, among other rights, all the income from the trust and principal distributions for her support, for the duration of her life. In addition, the wife was granted a testamentary limited power to appoint the trust assets remaining at her death to any person other than herself, her estate, or the creditors of either. The IRS ruled that the husband's estate was entitled to deduct the value of the wife's lifetime income interest and her right to principal distributions for her support, because these were transfers made to her for transfer tax purposes. No deduction was allowed, however, for the value of the wife's limited power of appointment, which she could exercise only in favor of persons other than herself, because the IRS considered this power a transfer of property made by the husband to the ultimate appointees and not a transfer to the wife as required for the exception under I.R.C. § 2043(b)(2) to apply. Conversely, the IRS ruled in Technical Advice Memorandum 9826002 (June 26, 1998) that a deduction was allowable for the full value of the trust property on the date of the husband's death when his former spouse was the only permissible recipient of trust income and principal and was granted a testamentary general power of appointment over the trust.

## **K. Federal Estate Tax: Deduction for Expenses, Indebtedness, and Taxes [§ 9.75]**

### **1. In General [§ 9.76]**

The deduction of funeral expenses, administration expenses, claims against the estate, unpaid mortgages, and other debts of the decedent for federal estate tax purposes is governed by I.R.C. § 2053. The test for deductibility rests on whether these items are allowable under state law.

### **2. Funeral and Last Illness Expenses [§ 9.77]**

With respect to last illness and funeral expenses of a deceased spouse, section 859.49 specifically provides that such expenses may be paid by the personal representative of a deceased spouse, and if so paid, must be allowed as a proper expenditure of the estate, even though the surviving spouse could have been held fully liable for the expense. Accordingly, all funeral and last illness expenses should be payable entirely by the estate and thus deductible in full from a deceased spouse's taxable estate. *Compare Estate of Lee v. Commissioner*, 11 T.C. 141 (1948) (holding funeral expenses fully deductible against decedent's estate under Idaho law), with *Pfeiffer v. United States*, 310 F. Supp. 392 (E.D. Cal. 1969) (holding only one-half of funeral expenses deductible since surviving spouse's one-half of community property was also subject to administration, and expenses were chargeable against entire community). Following the *Pfeiffer* decision, California changed its statute to make clear that the funeral and last illness expenses of a deceased spouse would not be charged to the community share of a surviving spouse. The effectiveness of this law change to permit full deductibility was recognized by the IRS in Revenue Ruling 71-168, 1971-1 C.B. 271. Subsequent changes in California law now require administration of only the decedent's one-half of community property. *See* Cal. Prob. Code § 11446 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 21 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot).



### 3. Administrative Expenses [§ 9.78]

Historically, in community property states, the entire community estate (i.e., both spouses' halves) was subject to administration when one of the spouses died. That rule has been modified by statute in California and Nevada so that only the decedent's interest in community property is subject to administration. UMPA § 18 cmt. Wisconsin follows the limited administration pattern of California and Nevada. Wis. Stat. §§ 857.01, 861.01(1).

In states that subject the entire community property estate to administration, normally only one-half of the administration expenses will be allowable as federal estate tax deductions, since the decedent's interest is in only one-half of the community property. See *United States v. Stapp*, 375 U.S. 118 (1963); *Lang's Estate v. Commissioner*, 97 F.2d 867 (9th Cir. 1938); *Estate of Lee v. Commissioner*, 11 T.C. 141 (1948); *Estate of Orcutt v. Commissioner*, 36 T.C.M. (CCH) 746 (1977). The IRS has ruled that the surviving spouse's share of expenses incurred for the production or collection of income or for management, conservation, or maintenance in conjunction with administering the community estate will be deductible for income tax purposes under I.R.C. § 212. Rev. Rul. 55-524, 1955-2 C.B. 535.

Even in situations in which the entire community property estate has been subject to administration, all attorney fees incurred in connection with the settlement of tax liabilities incurred by the decedent's portion of the estate have been held fully deductible by the estate. *Lang's Estate*, 97 F.2d 867 (applying Washington law).

With respect to Wisconsin law, section 857.04(1) provides that all general expenses of administration are to be paid out of the decedent's interests in marital property assets and in assets other than marital property on a pro rata basis according to the value of those interests. Accordingly, general administration expenses should be deductible in full by the estate.

Section 857.04(2) indicates that, to the extent possible, the personal representative must pay "special expenses" attributable to the management and control of marital property assets from the marital property assets generating those expenses and must pay special expenses attributable to the management and control of the decedent's other property from the other property. Under this latter provision, special

expenses relating to the management and control of marital property assets are properly allocated one-half to the decedent's interest and one-half to the surviving spouse's interest. *See infra* § 12.55. Therefore, only one-half of the special expenses attributable to marital property assets should be deductible by the deceased spouse's estate for federal estate tax purposes. *See, e.g., Stapf*, 375 U.S. 118; *Vaccaro v. United States*, 55 F. Supp. 932 (E.D. La. 1944), *aff'd on other grounds*, 149 F.2d 1014 (5th Cir. 1945).

A forced-election estate plan may cause the surviving spouse's one-half of community property or marital property assets to be included in the probate administration when it otherwise would not be under state law. Under such circumstances, the debts and expenses chargeable to the surviving spouse's half of the community property have been held not deductible as claims against the estate or expenses of administering the estate. *Stapf*, 375 U.S. 118. This was true even though the will directed the payment of all the debts and expenses out of the decedent's estate. *Id.*

#### **4. Debts and Claims [§ 9.79]**

Section 859.18 contains elaborate debt-satisfaction rules with respect to obligations existing at the death of a spouse. *See infra* §§ 12.80–131. It is likely that this state law scheme for the satisfaction of obligations at death will be determinative on the issue of deductibility of debts and claims for federal estate tax purposes. Accordingly, if a creditor is permitted to satisfy an obligation out of assets in a deceased spouse's estate and chooses to file a claim, amounts paid by the estate in satisfaction of the claim will be deductible for purposes of I.R.C. § 2053(a)(3), notwithstanding that the creditor might have satisfied the obligation in whole or in part out of assets of the surviving spouse. This follows from the fact that the Act contains no right of contribution as between spouses for family-purpose obligations. *See supra* § 8.36. Conversely, if the creditor's entire claim is satisfied by the surviving spouse, it is not clear whether some portion will be deductible under I.R.C. § 2053.

In other community property jurisdictions, the cases have held that since only one-half of community debts (as opposed to administration expenses and fees) are properly chargeable to the decedent's estate under general principles of community property law, only one-half may be

deducted. *Stapf*, 375 U.S. 118; *Lang's Estate*, 97 F.2d 867; Rev. Rul. 78-125, 1978-1 C.B. 292. Occasionally, this pattern has changed in cases in which different rules of debt satisfaction apply under state law. See, e.g., *Estate of Fulmer v. Commissioner*, 83 T.C. 302 (1984) (holding tort claims for shootings chargeable in their entirety against deceased husband's half of community property as his individual liability were deductible in full by his estate).

By the same token, separate debts of a decedent incurred or expended for the benefit of separate property are entirely chargeable against the decedent's separate estate and are also fully deductible for federal estate tax purposes. *Estate of Kerr v. Commissioner*, 14 T.C.M. (CCH) 178 (1955). The rationale of *Estate of Fulmer* and *Estate of Kerr* should apply to debts in Wisconsin that are not incurred in the interest of the marriage and the family, as well as to debts that were incurred before the determination date. See Wis. Stat. § 766.55(2)(c)1., 2., (d).

As indicated in section 9.78, *supra*, claims based on marriage agreements in which valuable community property rights are relinquished, or on property settlement agreements incident to divorce, may be deductible under I.R.C. § 2053(e) if the conditions of I.R.C. § 2043(b) and I.R.C. § 2516 are met.

## **L. Federal Estate Tax: Marital Deduction [§ 9.80]**

### **1. In General [§ 9.81]**

The federal estate tax contains an unlimited marital deduction for qualified interests in property that pass from a decedent to his or her surviving spouse. I.R.C. § 2056(a). For the purpose of determining deductibility, the federal estate tax marital deduction requires examination of the nature of the property interests transferred to the surviving spouse. To be deductible, the interest must be included in determining the value of the decedent's gross estate and must pass from the decedent to the surviving spouse. I.R.C. § 2056(a), (c). In addition, it must not be a "terminable interest" as described in I.R.C. § 2056(b) and Treasury Regulation § 20.2056(b)-1(b) and (c), or, if it is a terminable interest, it must be one that is deductible under Treasury Regulation § 20.2056(b)-1(d).

## 2. Terminable-interest Rule [§ 9.82]

Treasury Regulation § 20.2056(b)-1(b) defines a terminable interest as follows:

A “terminable interest” in property is an interest which will terminate or fail on the lapse of time or on the occurrence or the failure to occur of some contingency. Life estates, terms for years, annuities, patents and copyrights are therefore terminable interests. However, a bond, note, or similar contractual obligation, the discharge of which would not have the effect of an annuity or term for years, is not a terminable interest.

Under I.R.C. § 2056(b)(7), QTIP can qualify for the estate tax marital deduction if an appropriate election is made. Pursuant to the QTIP rules, the marital deduction is allowable for a surviving spouse’s life income interest in a trust, as long as the income must be distributed to the surviving spouse at least annually and the principal of the trust may not be appointed or distributed to any person other than the surviving spouse during his or her lifetime. Careful attention to the regulations under I.R.C. § 2056(b)(7) is necessary to ensure that the terminable-income interest passing to a surviving spouse under a QTIP trust will qualify for the estate tax marital deduction.

➤ **Caution.** It is not intended in this section to discuss the various types of property interests passing to a surviving spouse that will qualify for the federal estate tax marital deduction nor to discuss in detail the requirements that must be satisfied to qualify terminable-interest property for QTIP treatment. The marital deduction regulations are extensive, and the cases and literature on the subject are voluminous. Estate planning under the Act requires careful consideration of spousal arrangements to ensure that they qualify for the unlimited marital deduction. Failure to qualify an interest passing to a surviving spouse will result in that interest being taxable.

It is important to note that assets classified as the marital property of spouses, whether that classification occurs by operation of law, gift, written consent with respect to life insurance, marital property agreement, or court decree, will be treated as owned in equal shares by each of the spouses. Only one-half of each asset will be includible in the estate of the first spouse to die for planning purposes; conversely, the other half will be includible in the estate of the surviving spouse for

planning purposes. Estate planning considerations involving the marital deduction are discussed in chapter 10, *infra*.

The hazards of failing to create an interest that qualifies for the marital deduction are well illustrated by *Estate of Hedrick v. Commissioner*, No. 92-70785, 1994 WL 409713 (9th Cir. Aug. 5, 1994) (unpublished opinion), *rev'g* 64 T.C.M. (CCH) 249 (1992), an unpublished decision that involved the transfer of community property to a flawed joint revocable trust. The declaration of trust provided that the community and separate property of the decedent and his wife were to be held in trust during their joint lives and the life of the survivor. Upon the death of the survivor, all the property was to pass to charity. The declaration of trust failed to provide for any distribution of income to the surviving spouse during the survivorship period. It was unclear whether the trust could be revoked and the assets withdrawn by the survivor during his or her lifetime, a fact that was crucial to determination whether a marital deduction would be allowed, because in the absence of such a power of revocation, the trust would have constituted a terminable interest insofar as the decedent's wife was concerned. After a detailed consideration of the drafting history of the declaration of trust, the court held that the estate was entitled to a marital deduction for the decedent's share of community property transferred to the trust. The court concluded that the declaration of trust was ambiguous and was persuaded by extrinsic evidence that the spouses had intended that the trust remain revocable during the survivorship period and become irrevocable only upon the survivor's death.

Similar terminable-interest issues may arise when the spouses make arrangements for disposition of the spouses' property at the death of the survivor by a will substitute agreement that specifically provides that it is not amendable after the death of the first spouse. When a will substitute agreement is a third-party beneficiary contract, it likely will be regarded in the same light as joint, mutual, and contractual wills upon the death of the first spouse. Property transmitted to a surviving spouse subject to the terms of a joint, mutual, and contractual will has been held not to qualify for the marital deduction under I.R.C. § 2056. *See Batterton v. United States*, 406 F.2d 247 (5th Cir. 1968) (decided before the adoption of I.R.C. § 2056(b)(7)). Whether the interest passing to the surviving spouse under a will substitute agreement qualifies for the marital deduction depends on the rights and limitations to which the surviving spouse is subject under the terms of the agreement. Again, careful adherence to the QTIP rules of I.R.C. § 2056(b)(7) and the corresponding

Treasury regulations will be necessary if a marital deduction under that I.R.C. provision is desired.

If the terms of the will substitute agreement do not specifically negate the surviving spouse's right to amend the agreement with regard to the property to be disposed of at the surviving spouse's death, it is possible that the interest passing to the surviving spouse may qualify for the marital deduction under I.R.C. § 2056(b)(5) as a life estate coupled with a general power of appointment. *See* Treas. Reg. § 20.2056(b)-5(g). *But see Estate of Field v. Commissioner*, 40 T.C. 802 (1963); *Estate of Stockdick v. Phinney*, 65-2 U.S.T.C. (CCH) ¶ 12,351 (S.D. Tex. 1965); Tech. Adv. Mem. 9023004 (June 8, 1990). These cases and the ruling held that even though the surviving spouse under a Texas joint and mutual will had the power to use and consume the property or even give it away during her lifetime, the inability to appoint the entire property to herself or her estate necessitated the conclusion that the interest in property received by the surviving spouse did not qualify for the marital deduction under I.R.C. § 2056(b)(5). For a contrary result from a common law jurisdiction, see *Estate of Parry v. United States*, 91-2 U.S.T.C. (CCH) ¶ 60,075 (D. Utah 1991).

### **3. Interests Passing to Surviving Spouse by Elective Share [§ 9.83]**

Property elected by a surviving spouse under the augmented deferred marital property election of section 861.02 should be treated as nonterminable property passing to the surviving spouse and thus should qualify for the estate tax marital deduction.

The augmented deferred marital property election under section 861.02 allows a surviving spouse to elect to receive a one-half interest in the assets making up the couple's *augmented deferred marital property estate*, which consists of both spouse's probate and nonprobate deferred marital property, including transfers made to third parties within two years of the death of the first spouse to die. The surviving spouse's augmented deferred marital property election is satisfied with a pecuniary amount. The election presents two issues for purposes of determining whether the elective share qualifies for the federal estate tax marital deduction:

1. Whether the elective share received by the surviving spouse pursuant to the election is an interest in property passing from the deceased spouse to the surviving spouse for purposes of Treasury Regulation § 20.2056(c)-1(a); and
2. Whether the elective share is a nonterminable interest.

In cases in which the surviving spouse's election under state law is against the decedent spouse's will or other instrument, and the surviving spouse forfeits the benefits under the will or other instrument, the Treasury regulations take the position that the forfeited benefits (which presumably pass to others) are deemed not to pass from the decedent to the surviving spouse, and the interest to which the surviving spouse is otherwise entitled under state law is deemed to be substituted. Specifically, Treasury Regulation § 20.2056(c)-2(c) provides as follows:

*Effect of election by surviving spouse.* This paragraph contains rules applicable if the surviving spouse may elect between a property interest offered to her under the decedent's will or other instrument and a property interest to which she is otherwise entitled (such as dower, a right in the decedent's estate, or her interest under community property laws) of which adverse disposition was attempted by the decedent under the will or other instrument. If the surviving spouse elects to take against the will or other instrument, then the property interests offered thereunder are not considered as having "passed from the decedent to the surviving spouse" and the dower or other property interest retained by her is considered as having so passed (if it otherwise so qualifies under this section). If the surviving spouse elects to take under the will or other instrument, then the dower or other property interest relinquished by her is not considered as having "passed from the decedent to his surviving spouse" (irrespective of whether it otherwise comes within the definition stated in paragraph (a) of this section) and the interest taken under the will or other instrument is considered as having so passed (if it otherwise so qualifies).

This approach, whereby otherwise qualifying property interests actually received by a surviving spouse are treated as having passed from the decedent, thus qualifying them for the federal estate tax marital deduction, seems to apply in any situation in which the surviving spouse of a Wisconsin decedent is forced to make an equitable election under section 853.15. This approach could also be taken in situations in which an election is made in the decedent's will or other instrument.

The augmented deferred marital property election under section 861.02 is intended to provide protection for a surviving spouse when a significant portion of the couple's property consists of deferred marital property (for example, when the couple has moved to Wisconsin from a common law state). Thus, the amount elected by a surviving spouse is directly analogous to a support allowance or award. Treasury Regulation § 20.2056(c)-2(a) specifically recognizes that "[a]n allowance or award paid to a surviving spouse pursuant to local law for her support during the administration of the decedent's estate constitutes a property interest passing from the decedent to his surviving spouse."

Accordingly, such an allowance qualifies for the marital deduction if it is not a terminable interest. This is one possible analytical approach to the treatment of the amount elected by the surviving spouse under sections 861.02.

A number of cases have considered the terminable-interest treatment of a surviving spouse's elective interest in the deceased spouse's property. It has been held that even though the right of election is subject to formal actions in accordance with the requirements of local law or of the will, this fact does not prevent the interest passing to the surviving spouse from qualifying for the marital deduction. *Estate of Tompkins v. Commissioner*, 68 T.C. 912, 918 (1977); *Estate of Mackie v. Commissioner*, 64 T.C. 308, 311 (1975), *aff'd per curiam*, 545 F.2d 883 (4th Cir. 1976); *Hawaiian Trust Co. v. United States*, 412 F.2d 1313 (Ct. Cl. 1969); Tech. Adv. Mem. 8727002 (Mar. 16, 1987). The U.S. Tax Court, in *Estate of Mackie*, characterized rights of election by statute and those rights of election encompassed by a decedent's will as "a difference without a distinction." *Estate of Mackie*, 64 T.C. at 312. The fact that the surviving spouse might die before making the election did not result in the elected property being a terminable interest, because "once elected, the bequest is nonterminal and, therefore, deductible." *Estate of Tompkins*, 68 T.C. at 918.

Many estate plans drafted for Wisconsin couples will involve wills or revocable trusts making a provision for a surviving spouse, and further providing that the provision terminates (or is directly reduced) if the surviving spouse elects to receive property under section 861.02. Posing an election of benefits to a surviving spouse by itself does not disqualify the property offered as a terminable interest. Tech. Adv. Mem. 8735003 (May 10, 1987); Priv. Ltr. Rul. 9233033 (Aug. 14, 1992); Priv. Ltr. Rul. 9244020 (Oct. 30, 1992); Priv. Ltr. Rul. 9036040 (Sept. 7, 1990); Priv.



Ltr. Rul. 8936009 (Sept. 8, 1989) (all holding that interest passing to surviving spouse was not nondeductible terminable interest, notwithstanding that it was subject to condition that spouse not contest decedent's will).

In *Estate of Mackie*, 64 T.C. 308, the decedent's will bequeathed to his surviving spouse the right to select from his residuary estate properties that were sufficient to obtain the maximum allowable marital deduction. The will provided that the spouse could exercise the right to accept or reject the bequest in whole or in part by delivering a written statement to the personal representative within four months after the testator's death. The IRS contended that the bequest to the spouse was a nondeductible terminable interest, because persons other than the spouse would receive the property if and to the extent that she did not exercise the right of selection. It further contended that the requirement of acceptance of the bequest made the gift conditional. The Tax Court rejected these contentions and found that the surviving spouse had an absolute right to take outright a specified portion of the decedent's estate. Having exercised that right, she received property that passed to her from the decedent within the meaning of I.R.C. § 2056(a) and (c) and that did not constitute a terminable interest within the meaning of I.R.C. § 2056(b). *Id.* at 314.

Similarly, in *Estate of Neugass v. Commissioner*, 555 F.2d 322 (2d Cir. 1977), the surviving spouse was given a life estate in the decedent's entire art collection, coupled with a right to take absolute ownership of any item in the collection within six months following the decedent's death. The court held that the arrangement described alternative bequests, and that the surviving spouse's election to take absolute ownership clearly qualified for the marital deduction.

The posing of alternative bequests is closely analogous to an election to take against the will under state law. The surviving spouse in effect is put to a choice: take either provision A or provision B but not both. Treasury Regulation § 20.2056(c)-2(c) treats whatever interest is elected by the surviving spouse as having "passed from the decedent to the surviving spouse" and treats the relinquished interests as not having so passed. The logic of applying this position to "private" elections was adverted to in *Estate of Tompkins*, 68 T.C. 912, in which the United States Tax Court stated: "There is no substantial difference between an elective testamentary bequest of a nonterminable interest which relates back to the testator's death and a spouse's election against a will under

State law. Both qualify for the marital deduction so long as the interest actually passing is nonterminable.” *Id.* at 916; *see also Estate of Mackie*, 64 T.C. at 312; *Estate of Neugass*, 555 F.2d at 328.

This position was also followed in Revenue Ruling 82-184, 1982-2 C.B. 215, in which the IRS ruled that the marital deduction was available when the decedent gave his surviving spouse the choice of receiving a life income interest in a testamentary trust or an outright bequest of \$50,000 instead of the life income interest. The election had to be made within six months of death. Because the surviving spouse had the absolute right to elect to take a specific portion of the decedent’s estate (i.e., the \$50,000) within a reasonable time, and because that right arose at the moment of the decedent’s death, the spouse’s election of the \$50,000 was not a terminable interest and qualified for the marital deduction.

The crucial factor in Revenue Ruling 82-184 (as well as the cases cited) appears to be that the surviving spouse in each case elected to receive what in fact was a nonterminable outright interest in property. The requirement of making the election was viewed as a procedural requirement similar to making an election against the will under state law. The previously cited cases and rulings further demonstrate the desirability of having the estate planning documents provide that the election must be made within six months following the decedent’s death, which also prevents treatment of the interest received as a terminable interest. *See, e.g.*, Treas. Reg. § 20.2056(b)-3(b). Accordingly, there is substantial authority for the proposition that, in situations in which a testator or trust settlor gives his or her surviving spouse alternative elective provisions that must be exercised within six months of the testator’s or trust settlor’s death, and the provision actually elected by the surviving spouse provides a nonterminable interest, the marital deduction will be allowed for the property interests passing to the surviving spouse.

Is the augmented deferred marital property estate share elected by a surviving spouse under section 861.02 a terminable interest? It seems certain that the answer should be no. The size and extent of the surviving spouse’s election against the augmented deferred marital property estate under section 861.02 is fixed and ascertainable as of the moment of death of the first spouse to die. Only the ministerial task of classifying the couple’s assets is necessary before the election can be made. The surviving spouse alone (or his or her guardian) may exercise the election within six months after the deceased spouse’s death. Wis.

Stat. § 861.08(1). The surviving spouse receives a specific dollar amount that is not subject to divestiture upon subsequent remarriage and may be freely consumed by the surviving spouse during lifetime or disposed of by the surviving spouse at death. Accordingly, section 861.02 can be appropriately characterized as conferring an elective ownership interest in the surviving spouse in the deferred marital property subject to the election. It follows that the amount received under the section 861.02 augmented deferred marital property election should qualify for the marital deduction as other than a terminable interest.

Assuming that the augmented deferred marital property estate share received by a surviving spouse pursuant to section 861.02 is treated as a qualifying interest for purposes of the marital deduction, the question arises as to whether such share is subject to and will be reduced by estate taxes. This issue is important, because under I.R.C. § 2056(b)(4)(A), the marital deduction will be reduced for any federal or state death taxes payable out of qualifying interests passing to a surviving spouse.

Under section 861.05(3), the value of deferred marital property included in the augmented deferred marital property estate must be reduced by an equitable proportion of funeral and burial expenses, administrative expenses, other charges and fees, and enforceable claims. The Drafting Committee Notes to section 861.05(3), however, specifically provide that “[w]ith respect to ‘other charges and fees,’ it is expected that the property transferred under the election will qualify for the marital deduction and therefore should not bear any of the tax obligation of the estate.” See Howard S. Erlanger, *Wisconsin’s New Probate Code—A Handbook for Practitioners* app. C, at 45 (1998). Thus, the augmented deferred marital property estate share passes to the surviving spouse free of any federal or Wisconsin estate taxes imposed by reason of the deceased spouse’s death and should qualify in full for the marital deduction.

#### **4. Valuation of Encumbered Interests Passing to the Surviving Spouse [§ 9.84]**

Pursuant to I.R.C. § 2056(b)(4)(B) and Treasury Regulation § 20.2056(b)-4(b), if a property interest passing from the decedent to the surviving spouse is encumbered in any manner, or if the surviving spouse incurs an obligation imposed by the decedent in connection with the passing of the property interest, the value of the property interest

received by the surviving spouse is to be reduced by the amount of the obligation for purposes of determining the marital deduction. *See also United States v. Stapf*, 375 U.S. 118 (1963); Tech. Adv. Mem. 200131001 (Aug. 3, 2001) (holding that marital deduction for residue of wife's estate passing to husband must be reduced by amount transferred by husband to a trust after wife's death, when wife's will provided for diversion of residue to fund the trust, unless the husband funded trust with a specified amount).

Example (3) in Treasury Regulation § 20.2056(b)-4(b) sets forth the specific rule that, for purposes of computing the amount of the marital deduction in a forced-election estate planning situation, the value of property passing to the spouse that qualifies for the marital deduction is reduced by the value of any property relinquished by the surviving spouse. Thus, for example, the value of a decedent's assets passing to a qualifying trust created for the surviving spouse would typically be reduced by the value of the remainder interest in the surviving spouse's one-half of the community property transferred to that trust under the forced election.

The problem of reduction in the value of the marital deduction by the amount of an obligation imposed on a surviving spouse may also occur in situations other than forced-election estate plans. For example, assume that one spouse relinquishes substantial future marital property rights by executing an "opt-out" marital property agreement. The agreement requires the other spouse to make specific financial provisions at death for the first spouse. Is the value of an otherwise qualifying property interest passing to the first spouse under the other's estate planning documents reduced for marital deduction purposes following the death of the other spouse? The answer appears to be no, because the relinquishing spouse was not actually required to transfer any present and ascertainable property right, either at the time the agreement was entered into or later at the time of death. In support of this view, Revenue Ruling 68-271, 1968-1 C.B. 409, and Revenue Ruling 54-446, 1954-2 C.B. 303, hold that the relinquishment of marital rights by one spouse in the property or estate of the other in return for the other's contractual promise to make a financial provision by will is not adequate and full consideration sufficient to support a claim against the estate under I.R.C. § 2053, because of the express language of I.R.C. § 2043(b). However, the value of property to which the surviving spouse is entitled under the agreement (or under a will executed to effectuate it) is deemed to have

passed from the decedent to the surviving spouse and will qualify for the marital deduction if all other statutory requirements are satisfied. *Id.*

However, in the context of claims made under I.R.C. § 2053 with respect to rights arising under a marriage agreement, *Estate of Carli v. Commissioner*, 84 T.C. 649 (1985), held that when the spouses executed a premarital agreement in which the wife relinquished her presently enforceable community property rights in the husband's earned income, the relinquishment was adequate and full consideration for purposes of supporting a claim against the husband's estate under I.R.C. § 2053. This was true even though a mathematically accurate determination of the present value of the relinquished community interests was impossible when the agreement was entered into. The United States Tax Court presumed the value of the property interests exchanged under the premarital agreement to be equal through application of the rule it had previously adopted in *Estate of O'Nan v. Commissioner*, 47 T.C. 648, 663 (1967). See also *United States v. Davis*, 370 U.S. 65 (1962); *Philadelphia Park Amusement Co. v. United States*, 126 F. Supp. 184 (Ct. Cl. 1954). The logical extension of the rationale of *Estate of Carli* is that surrender of presently enforceable marital property rights by one spouse in the assets or future acquisitions of the other is an obligation equal in value to the financial provision received by the survivor. By virtue of Treasury Regulation § 20.2056(b)-4(b), this may have the effect of reducing the marital property deduction to zero and replacing it with a claims deduction under I.R.C. § 2053 for the value of the property to which the surviving spouse is entitled under the agreement.

## **M. Federal Gift Tax: Gift Transactions and Completed Gifts [§ 9.85]**

### **1. In General [§ 9.86]**

The federal gift tax is imposed on transfers of property by any individual. I.R.C. § 2501(a)(1). It is immaterial whether the transfer is in trust or otherwise, whether the gift is direct or indirect, or whether the property is real or personal, tangible or intangible. I.R.C. § 2511(a). Donative intent is irrelevant to the federal gift tax. If a gift of marital property is made to a third person, the gift is treated for federal gift tax purposes as made one-half by each spouse. For example, a gift of \$100,000 of marital property is considered a gift of \$50,000 by each

spouse, and each spouse must file a federal gift tax return. *See* Instructions to Form 709 (U.S. Gift and Generation-Skipping Transfer Tax Return).

For purposes of the federal gift tax law, a gift is not deemed complete until the donor's dominion and control ceases. Treas. Reg. § 25.2511-2(b). The gift tax regulations state that a gift is incomplete "in every instance in which a donor reserves the power to revest the beneficial title to the property in himself." Treas. Reg. § 25.2511-2(c). Therefore, the question of when certain gifts of marital property assets are deemed to be complete as a matter of state property law under the Act will thus be relevant in considering federal gift tax questions under the regulations.

Under section 766.51(4), the right to manage and control marital property assets permits gifts of that property subject to the remedies in chapter 766. The 1985 Trailer Bill Supplemental Nontax Note to section 766.51(4) states as follows:

[The] amendment clarifies that a gift of marital property to a [third] person by a spouse who has the right to manage and control the marital property is "subject to remedies provided under ch. 766". The revised language replaces the rule that the right to manage and control marital property permits gifts of that property "only to the extent provided in s. 766.53." The revised language assumes that, even if a remedy is available, the gift was made when the transfer occurred.

This language was intended to make clear that if a spouse has the right of management and control with respect to a marital property asset and makes a gift of it to someone else, the gift is complete when made; the nondonor spouse's rights in the asset are extinguished subject only to remedies granted under section 766.70 and other provisions of chapter 766. *See* chapter 8, *supra*, for further discussion of remedies.

Under section 766.53, a spouse who has the right to manage and control marital property assets may, acting alone, give a third person marital property assets if the amount given to the third person does not aggregate more than either \$1,000 in a calendar year, or a larger amount if, when made, the gift is reasonable in amount considering the economic position of the spouses. No consent or joinder of the other spouse is necessary for such gifts, and no remedies arise in the other spouse with respect to such gifts. If, however, the amount of the gift exceeds the statutory limits in section 766.53, and both spouses do not "act together"

in making the gift, the nondonor spouse has remedies under section 766.70(6) against the donor spouse, the gift recipient, or both. As to what constitutes “acting together,” the 1985 Trailer Bill Supplemental Nontax Note to section 766.53 concludes as follows on the subject:

The rule does not require spouses to act simultaneously to be considered acting together; subsequent consent by the other spouse is sufficient. It is assumed that common law doctrines regarding consent, such as estoppel and ratification, apply. Further, it is assumed that, if subsequently consented to by a spouse, the gift was made when the original transfer occurred.

An action under section 766.70(6)(b) may seek to recover either the property that was the subject of the gift or a compensatory judgment equal to the amount by which the gift exceeded the statutory limits. If the recovery occurs during marriage, it is marital property; if it occurs after dissolution or the death of either spouse, it is limited to 50% of the former marital property and is the separate property of the recovering spouse. The nondonor spouse must commence the action within the earliest of (1) one year after he or she has notice of the gift; (2) one year after a dissolution of the marriage; or (3) the end of the period for filing claims under section 859.01 after the death of either spouse. Wis. Stat. § 766.70(6)(a). In certain cases involving unilateral transfers of marital property assets that are complete transfers during the life of the donor spouse, the other spouse may recover his or her one-half of the marital property assets from the gift recipients, but no later than one year after the first to occur of the donor spouse’s death or the nondonor spouse’s death. Wis. Stat. § 766.70(6)(b). The general rules concerning gifts to third parties are discussed in detail in section 4.36, *supra*.

➤ **Note.** In the following discussion, it is assumed that a unilateral gift of a marital property asset has been made by a spouse having the right of management and control, that the gift exceeds the statutory limits in section 766.53, and that there is no “acting together” in making it. The term *nondonor spouse* is used to refer to the spouse who does not have management and control rights with respect to the marital property asset that is the subject of the gift and who does not act together with the donor spouse in making it.

When the conditions of section 766.53 are not met, the nondonor spouse has statutory remedies. Two related questions will arise at this point for purposes of the federal gift tax. The first is when the gift of a marital property asset made by the donor spouse is deemed complete.

Section 766.51(4) clearly establishes that the gift of the entire marital property asset is made when the transfer occurs. *See* 1985 Trailer Bill Supplemental Nontax Note to section 766.51(4). The issue is whether the nondonor spouse's right to recover all or part of the asset as one of the remedies under section 766.70 is the same as a power reserved in the nondonor to revest the beneficial title to the property in himself or herself for purposes of Treasury Regulation § 25.2511-2(c). If it is, then as to the nondonor spouse's interest in the marital property asset, the gift would be incomplete until the statute of limitation for exercising the remedy expires. If it is not, then the gift will be complete when the transfer by the donor spouse occurs. The remedies under section 766.70 are all contingent on the exercise of judicial discretion and are not limited solely to recovery of the gift property from the donee. It seems probable that these remedies will not be regarded as being the same as an automatic and unfettered right on the part of the nondonor spouse to revest in himself or herself the beneficial title to all or part of the transferred marital property asset.

If, however, a unilateral gift of a marital property asset valued in excess of the statutory limits of section 766.53 is made when the spouses do not act together, and the gift is deemed to be incomplete for federal gift tax purposes (at least as to the portion subject to the nondonor spouse's remedy of recovery), a second question arises: has the nondonor spouse made a gift if he or she fails or refuses to invoke remedies under section 766.70? The issue is whether the acquiescence of the nondonor spouse under those circumstances, in itself, results in a gift of his or her marital property interest to the third parties.

These questions will have an impact in at least three situations: (1) outright gifts to individual parties, (2) outright gifts to charities, and (3) gifts in trust for the whole or partial benefit of third parties. Each of these situations will be dealt with separately.

## **2. Outright Gifts to Individuals [§ 9.87]**

For the reasons discussed in section 9.86, *supra*, it appears that an outright unilateral gift of a marital property asset to an individual by a spouse having the right of management and control will be deemed complete for federal gift tax purposes when made. *See* Wis. Stat. § 766.51(4).



There is an admitted scarcity of authority on this question. One decision, however, bears indirectly on the issue by looking at the quantum of estate possessed by a nonconsenting spouse in the gifted property. In *Estate of Lucey v. Commissioner*, 13 T.C. 1010 (1949), the court upheld the commissioner's contention that, because the deceased wife had the right to revoke a gift unless the gift could be shown not to have been made in fraud of her rights, and no such showing was made, it would be proper to include one-half of the gift in her estate. The gift in question was the bargain sale of community property oil leases by the husband to a corporation that he owned as his separate property. The right to revoke the gift was asserted as the basis for inclusion of the community property interest in the estate of the nonconsenting spouse. If this position is tenable, then it would follow that there is no completed transfer to the donee as long as the nonconsenting spouse's complete right to revoke exists.

However, the right to revoke in *Estate of Lucey* is to be contrasted with the remedies afforded a nonconsenting spouse under section 766.70. Those remedies may be asserted against parties other than the donee (i.e., the donor) and against property other than the gifted property (i.e., a compensatory money judgment); they are not an absolute and unfettered right, because they must be granted by a court of law, consistent with procedural due process. As a result, they only remotely resemble reserved property rights of the kind described in Treasury Regulation § 25.2511-2(c).

To the extent that the donor spouse's unilateral gift of a marital property asset for any reason does not constitute a completed gift of the nondonor spouse's marital property interest, it seems clear that a gift by the nondonor spouse nonetheless will be deemed to occur if the nondonor does not take timely action to recover the marital property asset after receiving notice of the gift or within the applicable statutory time periods following dissolution of the marriage or the death of either spouse. Acquiescence by a nondonor spouse in a transfer of community property assets to third parties has been deemed to be a gift transfer of that spouse's one-half interest to the transferees. See *Whiteley v. United States*, 214 F. Supp. 489 (W.D. Wash. 1963).

➤ **Practice Tip.** If the gift is sufficiently large to require the filing of federal gift tax returns, and the nondonor spouse either executes a return reporting a gift of his or her one-half interest in the property or executes a consent to gift-splitting on the federal gift tax return of the

donor spouse (*see infra* § 9.99), there has probably been an “acting together” with respect to the making of the gift, which should relate back to the date of the gift. *See* 1985 Trailer Bill Supplemental Nontax Note to section 766.53. This should estop the nondonor spouse from later invoking remedies potentially available under section 766.70.

### **3. Outright Gifts to Charity [§ 9.88]**

In theory, outright gifts to individuals (*see supra* § 9.87) and outright unilateral gifts to charity present similar issues, although no decided cases on the subject have been ascertained. The IRS apparently has not disallowed deductions for unilaterally made charitable contributions on joint income tax returns in community property states. Several reasons are suggested.

The first is that the vast majority of charitable contributions of married persons will be reported on joint income tax returns. Many taxpayers itemize their charitable gifts on Schedule A to Form 1040. Accordingly, if the nondonor spouse signs a joint income tax return that specifically describes the charitable contribution, that should evidence sufficient consent to constitute “acting together” in making the gift. The consent can properly be deemed to relate back to the date of the gift. *See* 1985 Trailer Bill Supplemental Nontax Note to section 766.53.

The second reason why charitable contributions made by a spouse with management and control should be deemed completed when made, for income tax purposes, is that the tax benefit rule is available to prevent revenue losses. If a deduction is claimed in one year, and the nondonor spouse subsequently attempts to recover the gift (assuming that his or her execution of a joint income tax return was not a sufficient consent to constitute “acting together” in making the gift), the recovered amount quite clearly would be subject to inclusion in the gross income of the spouses for the year of recovery under the tax benefit rule if it had reduced income subject to tax in the earlier year. *See* I.R.C. § 111(a); *see also* Rev. Rul. 76-150, 1976-1 C.B. 38.

Third, the Wisconsin statutory scheme that accords a spouse with management and control rights the power to make unilateral gifts of marital property assets (subject only to the nondonor spouse’s judicial

remedies) adds a further argument in favor of deductibility of charitable gifts when made. *See* Wis. Stat. § 766.51(4); *see also supra* § 9.80.

The *Tax Practitioner Newsletter* (Apr. 1988) of the District Director of the IRS, Milwaukee District, states the director's view that if a nondonor spouse signs a joint income tax return on which a gift of marital property assets is claimed as a charitable deduction, the nondonor's action in signing the return should be treated as a ratification or affirmation of the gift. That view raises the question whether the gift will be regarded as complete for tax purposes at the time of ratification (normally in a subsequent taxable year) or at the time the gift was in fact made. For further discussion, see DOR Publ'n 113, *supra* § 9.6, at 21.

It is not completely clear whether the IRS agrees that the nondonor spouse's statutory remedies in section 766.70(6) are not the same as an absolute property law right to revest the beneficial title to the donated marital property assets in the spouses or otherwise to revoke the gift. The discussion in DOR Publication 113, *supra* § 9.6, at 21, about the federal treatment of charitable gifts made by one spouse, is premised on the view that if one year passes after the nonconsenting spouse became aware of the gift, and that spouse took no steps to set it aside, the gift is deemed complete at that time. *See* Wis. Stat. § 766.70(6)(a). However, the legislative history to section 766.51(4), discussed in section 9.86, *supra*, makes it clear that a gift of a marital property asset made by a spouse having the right to manage and control the property is complete when made. All these factors would argue rather strongly against an IRS position that charitable gifts of marital property assets by one spouse are not completed when made.

➤ **Practice Tip.** The *Tax Practitioner Newsletter* suggests that, in many instances, the question of when the gift is complete will not be an issue, particularly if it is essentially a "timing question"—in other words, the question is not whether the charitable contribution deduction will be allowed, but only in which taxable year it will be allowed. The *Tax Practitioner Newsletter* suggests that "if the particular tax situation is similar in both years, it would not be appropriate for an audit adjustment to be made to shift the gift to the technically correct year."

## 4. Gifts in Trust to Third Parties [§ 9.89]

### a. In General [§ 9.90]

Perhaps the most difficult situations involving completion of gifts are posed by unilateral transfers of marital property assets in trust. This is the result of the uneasy interface between the gift-recovery statute (section 766.70(6)) and the classification statute that provides that a transfer of marital property assets to a trust does not, “by itself,” reclassify the property. Wis. Stat. § 766.31(5). The interrelationship of those sections with respect to marital property assets transferred in trust by one or both spouses is discussed in detail in sections 2.102 and 4.36, *supra*. These statutes appear to apply regardless of whether the transfer is to a trust that is revocable by one or both parties, or to a trust that is (or becomes) irrevocable.

### b. Revocable Trusts [§ 9.91]

For reasons discussed in section 9.65, *supra*, section 766.31(5) should control to prevent the completion of any unilateral gift to a third party of marital property assets placed in a revocable living trust during the joint lifetimes of the spouses, unless the revocable trust instrument meets all the requirements of a marital property agreement under section 766.58 and has the effect of reclassifying the transferred property or creating vested interests. The comment to section 4 of UMPA makes clear that the rule of section 766.31(5) is intended to apply to revocable trusts. A unilateral gift of marital property assets in trust by a spouse possessing the right of management and control, even when the settlor spouse reserves the sole right to revoke the trust during his or her lifetime, should not destroy the marital property character of the trust assets during the joint lifetimes of the spouses. *See Katz v. United States*, 382 F.2d 723 (9th Cir. 1967).

Upon the death of one of the spouses, however, if no further right to revoke the trust in whole or in part is retained by the survivor, a gift of the survivor’s share in the marital property assets will occur to any third-party beneficiaries of the trust. *Commissioner v. Chase Manhattan Bank*, 259 F.2d 231 (5th Cir. 1958). This gift will be deemed completed, at the latest, upon expiration of the survivor’s (or the survivor’s personal

representative's) right to recover the survivor's share of the marital property assets as specified in section 766.70(6)(b).

### **c. Irrevocable Trusts [§ 9.92]**

Section 766.31(5) is neutral on its face, applying equally to transfers to irrevocable trusts as well as to revocable trusts. However, the “by itself” language of the statute implies that the fact of irrevocability, of joinder by both spouses, or of other elements, may bring about an immediate reclassification of marital property assets transferred to the trust, at least for property law purposes. *See supra* § 2.102.

If the irrevocability of a trust (even a trust granting the nonsettlor spouse an income or remainder interest) is sufficient to cause an immediate reclassification of marital property assets placed in the trust and thus to cause a gift of the vested interests passing to third-party beneficiaries of the trust, the gift of the marital property interests passing to third-party beneficiaries would be complete for federal gift tax purposes when the assets are transferred to the trust. *See supra* § 2.102.

If the irrevocable gift in trust is exclusively for the benefit of third parties, a reading of sections 766.31(5) and 766.51(4) leads to the conclusion that there is an immediate reclassification of the marital property assets placed in the trust. *See supra* § 2.101. This follows logically, because the managing spouse who is the settlor of the irrevocable trust could have made the same transfer outright to the donees as a completed gift, subject only to the nondonor's spousal remedies under section 766.70(6)(a). *See Wis. Stat. § 766.51(4)*. The immediate reclassification of the marital property assets at the time of the transfer in trust should constitute a completed gift to the third parties of both spouses' interests in the marital property asset. *See supra* § 2.102.

The leading case involving completion of unilateral gifts of community property assets in trust superficially appears to support a contrary view, but only because the nondonor spouse had an absolute statutory power of revocation. In *Harper v. Commissioner*, 6 T.C. 230 (1946), an income tax case, the tax court held that a gift of community property assets to an irrevocable trust by the husband did not constitute a completed gift under California law as long as the statute of limitation on the wife's statutory power to revoke the gift had not expired, unless the wife had given her prior written consent to the gift. Under the applicable

California law, the assets transferred in trust vested immediately in the donees, subject only to revocation of the gift by the wife and reinstatement of the assets as part of the community property.

Under Wisconsin law, a typical transfer of marital property assets to an irrevocable trust for the benefit of third parties will constitute a completed gift when made under section 766.51(4) unless circumstances suggest that reclassification and transfer of the property was not intended. *See supra* § 2.102. The nondonor spouse has no absolute right of revocation or recovery that can be exercised against the assets in the trust, but has statutory remedies that are invoked by commencing a court action against either the donor spouse or the donees. *See Wis. Stat. § 766.70(6)(a).*

The issue of completion of unilateral gifts of marital property assets in trust is further complicated when the irrevocable trust holds life insurance policies on the life of the settlor. In those circumstances, if reclassification does not take place immediately upon the transfer (and it is believed that it does), and further, if marital property funds are used to pay premiums, all or a portion of the life insurance policies and proceeds will be classified as marital property under subsections 766.61(3)(d) and (f). *See supra* § 2.177; *see also supra* § 9.59 (for possible federal estate tax consequences). If life insurance paid for in part with marital property funds is one of the assets of the irrevocable trust, and the insured settlor dies, it is not clear whether the surviving spouse's remedies to reach the proceeds are subject to the short limitation period in section 766.70(6)(a) or the longer limitation period in section 766.70(6)(b). At the latest, a gift of the nondonor spouse's marital property interest in the trust to third-party beneficiaries becomes complete when the appropriate limitation period for commencing an action to recover that interest in the trust property expires. It is clear that when the surviving spouse's right to recover the marital portion of the proceeds expires, the gift to third parties is complete for federal transfer tax purposes. *Whiteley v. United States*, 214 F. Supp. 489, 493 (W.D. Wash. 1963).

If, for some reason, there is no reclassification of marital property assets transferred into an irrevocable trust for the benefit of third parties, and if the nondonor spouse dies before the death of the settlor spouse and before the applicable limitation period in section 766.70(6) has run, it appears that the remedy survives and may be exercised by the nondonor spouse's personal representative or special administrator until the limitation period expires. This right of action may properly be regarded

as an unliquidated claim or cause of action includible in the deceased nondonor spouse's gross estate under I.R.C. § 2033. *See, e.g., Estate of Houston v. Commissioner*, 44 T.C.M. (CCH) 284 (1982). Because the nondonor spouse does not have an absolute right of recovery, it is unlikely that he or she will be deemed to have a power of revocation under I.R.C. § 2038 with respect to one-half of any marital property asset in the trust, as was the case in *Estate of Lucey v. Commissioner*, 13 T.C. 1010 (1949). *See also supra* § 9.65. The same result would follow if the nondonor spouse died after the settlor spouse, but before the statute of limitation for recovery of gifts in section 766.70(6) had expired.

➤ **Practice Tip.** The foregoing discussion underscores the desirability of having the spouses act together in making large gifts to third parties, whether outright or in trust, since it achieves the highest degree of certainty with regard to the completion of gifts for tax purposes.

## **5. Gifts at the Death of One Spouse to Third Parties Under Will Substitute Agreements [§ 9.93]**

There is a significant gift tax concern that could affect the use of will substitute agreements (*see supra* §§ 7.99–106) that purport to transfer the spouses' property to third persons at the death of the surviving spouse. In *Pyle v. United States*, 766 F.2d 1141 (7th Cir. 1985), the taxpayer and her husband executed a joint and mutual (i.e., contractual) will that purportedly gave each other a fee simple in all their property but that went on to spell out in great detail how their property was to be disposed at the death of the surviving spouse. The joint and mutual will imposed significant constraints on the survivor's ability to invade or dispose of the property during the survivor's lifetime. These restrictions were deemed to constitute an ascertainable standard for invasion under state law. Under these circumstances, the court found that when the survivor died, the contract became binding and a completed gift resulted to the third-party remaindermen named in the joint and mutual will.

The quandary posed for Wisconsin residents desiring to use a will substitute agreement is that section 766.58(3)(f) provides that, when a will substitute agreement purports to dispose of the spouses' property without probate at the death of the survivor, the surviving spouse may amend the will substitute agreement at any time after the death of the

first spouse with regard to property to be disposed of at the survivor's death, unless the will substitute agreement expressly provides otherwise. According to the 1985 Trailer Bill Original Nontax Note to section 766.58(3)(f), this provision is designed to avoid unintended hardship because of changed circumstances when the surviving spouse survives the deceased spouse for a substantial period of time. The provision implies that the surviving spouse may amend the terms of the agreement to allow the spouse to invade and consume the property or even assign the property to other persons.

Since many spouses who enter into will substitute agreements disposing of property at the death of the survivor will want assurance that the property will pass to the intended third-party beneficiaries and will not be diverted by the surviving spouse, it is likely that many such agreements will be drafted to provide either that they cannot be amended, or that invasion or consumption of the property by the survivor is strictly limited by an ascertainable standard. If an agreement is so limited and cannot be amended by the surviving spouse, then it appears to fall squarely within the *Pyle* holding, and completed gifts to third-party beneficiaries will result at the death of the first spouse.

Although there may be reasons for drafting will substitute agreements so that they cannot be amended or so that invasion or consumption of the property by the surviving spouse is limited by an ascertainable standard, it is worth noting that not including such provisions would appear to avoid gift tax liability for completed gifts to third-party beneficiaries at the death of the first spouse. *Estate of Lidbury v. Commissioner*, 800 F.2d 649 (7th Cir. 1986), involved a joint and contractual will executed by Illinois residents. However, unlike *Pyle*, 766 F.2d 1141, and a similar case, *Grimes v. Commissioner*, 851 F.2d 1005 (7th Cir. 1988), also involving Illinois law, the survivor in *Lidbury* was free to consume the spouses' property entirely during his lifetime; thus, the amount of property to which the Lidburys' children were entitled under the contractual will was too uncertain to trigger a gift tax at the death of the first spouse. Accordingly, it seems that a will substitute agreement that is drafted either to permit invasion or consumption of the property subject to the agreement by the surviving spouse, or to permit the survivor to amend the agreement as described in section 766.58(3)(f), should eliminate the possibility of a taxable gift at the death of the first spouse.



## 6. Relinquishment of Community Property Rights [§ 9.94]

A taxable gift may also occur in cases in which a surviving spouse relinquishes community property rights or no longer has a legal right to recover them. A common example is when a surviving spouse fails to claim his or her community property share of insurance proceeds, thus permitting them to pass to a trust in which the surviving spouse has a life estate. It has been said that “[the] election not to claim is in practical effect a transfer to others.” *Whiteley*, 214 F. Supp. at 493. See also *Commissioner v. Chase Manhattan Bank*, 259 F.2d 231 (5th Cir. 1958), in which a completed gift was deemed to occur when insurance proceeds passed to an insurance trust at the husband’s death, and the surviving wife had no legal right to recover her share from the trustee in the absence of fraud. That case also involved a deemed gift by the surviving wife of her community share of assets held in a revocable trust created by her husband. The trust was revocable solely by the husband during his lifetime, and the gift was held to occur upon his death. In both fact situations, the value of the gift is the value of the assets transferred, reduced by the life income interest retained by the survivor.

Execution of a written consent under section 766.61(3)(e) raises similar issues about relinquishment of marital property rights, either in property used to pay premiums on a life insurance policy or in the ownership interest or proceeds of the policy. To the extent provided, written consent can be used not only to consent to the designation of a beneficiary but also to relinquish or reclassify either all or a portion of the consenting spouse’s interest in the ownership interest and proceeds of the policy. If the wife names her son as beneficiary of a life insurance policy insuring her life and designating her as owner, and the husband makes a written consent, the consent can provide that the husband relinquishes his rights not only to the insurance proceeds when his wife dies, but also to all other ownership interests in the policy and proceeds as well, without regard to the classification of marital property assets used by the wife or another person to pay premiums.

The husband’s consent could also state that the policy (and assets used to pay premiums as well) is reclassified as the wife’s individual property, even if premiums are subsequently paid from other classifications of property. For federal gift tax purposes, the reclassification features of the written consent may result in a gift of the

husband's present marital property interest in the policy to the wife, valued as of the date of the consent. Further completed gifts will occur as premium payments are made from marital property assets and as cash values are added to the policy each year. These gifts should qualify for the marital deduction. If the written consent is irrevocable, it should follow that, because the husband made a gift to his wife at the time of the consent (or at the time of premium payments or the crediting of cash values), he would not be treated as making a gift to the third-party beneficiary when his wife dies.

With respect to *revocable* consents, section 766.61(3)(e) provides that unless the written consent provides otherwise, revocation does not operate retroactively to change the classification of any marital property assets that were already reclassified by the consent or in which the revoking spouse had previously relinquished an interest. This could result in a mixed bag of completed and uncompleted gifts. If the consent in the foregoing example were revocable and if the husband chose to revoke it, his relinquishment of either a marital property interest in property used by the wife to pay premiums or in cash value increases in the policy during the period before the revocation would nonetheless remain completed gifts to her. In addition, a revocable consent should effectively "purify" the policy of the husband's other ownership interest in the policy up to the point when the consent was revoked. Following revocation, a marital property component in the policy may be revived to the extent that the general classification rules in section 766.61 once again apply.

## **N. Federal Gift Tax: Valuation [§ 9.95]**

### **1. In General [§ 9.96]**

The general federal gift tax valuation rules in I.R.C. § 2512(a) and Treasury Regulation §§ 25.2512-1 to .2512-9 parallel those of the federal estate tax discussed at section 9.56, *supra*. Consistent with the idea that donative intent is not required for a taxable gift, I.R.C. § 2512(b), dealing with valuation of gifts, provides that if property is transferred for less than an adequate and full consideration in money or money's worth, the excess of the value of the property transferred over the value of the consideration received is deemed a gift.

## 2. Forced-election Transfers [§ 9.97]

Forced-election estate plan situations may involve “bargain sale” gifts. The federal estate tax consequences are discussed in section 9.73, *supra*.

As discussed in section 9.73, *supra*, there has been much debate among the federal circuit courts of appeal over whether the consideration deemed to have been transferred by the surviving spouse in a forced-election plan should be measured by the value of his or her remainder interest in the community property transferred (because the surviving spouse retains a life income interest in that property in addition to receiving a life interest in the deceased spouse’s half of the community property) or by the full, undiminished value of his or her one-half interest in the community property transferred. *Compare Gradow*, 11 Cl. Ct. 808 (holding that consideration flowing from surviving spouse consists of his or her full one-half interest in community property transferred), *with Estate of D’Ambrosio*, 101 F.3d 309 (holding that consideration flowing from surviving spouse should be measured by actuarial value of remainder interest in community property transferred). This determination is important, because the surviving spouse will be considered to have made a taxable gift to the remaindermen to the extent that the consideration deemed given by the surviving spouse under the forced-election plan is greater than the discounted present value of the life income interest received in the decedent’s one-half of the community property.

It may also be the case that a different valuation test applies in forced-election estate plans for gift tax purposes than for estate tax purposes, because of the operation of I.R.C. § 2702. Under section 2702, it would appear that the value of the surviving spouse’s retained income interest in his or her half of the community property should be disregarded if the remainder interest passes to members of his or her family (generally lineal descendants and siblings and their spouses). Consequently, the surviving spouse would be treated as having made a gift of the entire value of his or her share of the community property, less only the value of the life interest received from the deceased spouse’s share. The operation of section 2702 is described in Treasury Regulation § 25.2702-1(b) as follows:

Effect of Section 2702. If Section 2702 applies to a transfer, the value of any interest in the trust retained by the transferor or any applicable family

member is determined under § 25.2702-2(b). The amount of the gift, if any, is determined by subtracting the value of any interests retained by the transferor or any applicable family member from the value of the transferred property. If the retained interest is not a qualified interest ..., the retained interest is generally valued at zero, and the amount of the gift is the entire value of the property.

The result of I.R.C. § 2702 with respect to retained interests other than qualified interests (fixed annuities or unitrust amounts) is consistent with the approach taken in *Gradow*—namely, that the determination whether the surviving spouse has received full consideration is made by comparing the total value of the property transferred to the actuarially determined value of the life income interest received in the deceased spouse's property.

It should be noted that I.R.C. § 2702 will not apply if the remainder beneficiaries are not members of the surviving spouse's family. The rule for valuation of a gift under such circumstances is illustrated by *Commissioner v. Siegel*, 250 F.2d 339 (9th Cir. 1957), and *Estate of Bressani v. Commissioner*, 45 T.C. 373 (1966). In each of these cases, the value of the surviving widow's gift to the remainder beneficiaries was the value of her one-half of the community property assets passing to her husband's trust less the value of her retained life estate in that one-half, reduced by the value of the life estate she received in the decedent's one-half of the community property assets that were retained in the trust.

*Robinson v. Commissioner*, 675 F.2d 774 (5th Cir. 1982), *aff'g* 75 T.C. 346 (1980), provides an interesting variation on the forced-election theme. The court held that the completed gift of the surviving spouse's remainder interest did not occur until she released a limited power of appointment over the remainder that was granted to her under the terms of the trust for her benefit under her husband's will. The existence of the limited power prevented the wife's election to take under the will and the resultant transfer of her half of the community property to the trust from being treated as a completed gift at the time of the husband's death. Treas. Reg. § 25.2511-2(c). As a result, however, she was unable to reduce the value of her gift by the value of the life estate she had received several years earlier in her deceased husband's half of the community property. In the court's view, the earlier consideration (i.e., the receipt of a life estate) was not consideration for her wholly gratuitous subsequent release of the limited power of appointment.

### 3. Minority-interest Discounts [§ 9.98]

The minority-interest and fractional-interest discount issues involving marital property interests in closely held stock and real estate are discussed in detail in section 9.56, *supra*. The position of the IRS for federal gift tax purposes is set forth in Revenue Ruling 93-12, 1993-1 C.B. 202. As discussed in section 9.56, *supra*, discounts should be allowed for each spouse's one-half share of marital property that is gifted to a third party.

### O. Federal Gift Tax: Gift Reporting and Gift Splitting in Gifts by Husband or Wife to Third Parties [§ 9.99]

Under the Act, each of the spouses owns an undivided 50% interest in each item of marital property. Wis. Stat. § 766.31(3). Accordingly, each spouse will be required to file a federal gift tax return for the value of his or her half of any marital property asset transferred by gift, if the value of that one-half exceeds \$13,000 (the annual gift tax exclusion amount under I.R.C. § 2503(b) for 2010) to any donee in any calendar year. For example, assume that a marital property asset with a value of \$30,000 is under the exclusive management and control of one spouse, and that the property is given outright by the managing spouse to a child. Further, assume that the other spouse has no objection to that gift and in fact concurs in it. Each spouse would file a federal gift tax return reporting a \$15,000 gift of his or her respective one-half interest in the asset. The taxable portion of such gift would be \$2,000 after applying the \$13,000 annual exclusion.

If the nondonor spouse does not agree to the gift, he or she should not be obligated to file a federal gift tax return with respect to his or her one-half of the transfer, particularly if the nondonor invokes (or intends to invoke) the remedies in section 766.70(6) by commencing a timely action. The danger for a nonconsenting nondonor spouse who files a federal gift tax return is that the return might be viewed as a ratification of the gift or an “acting together” with the donor spouse. *See supra* § 9.86.

Assuming that no other gifts are made by the spouses, if the total of the marital property assets transferred to the donee is, for example, \$20,000, no federal gift tax returns would be required of either spouse

because the respective gifts of each (\$10,000) are less than the \$13,000 annual exclusion. *See* I.R.C. §§ 2503(b), 6019(a). However, the \$13,000 annual exclusion does not apply to transfers that are not present interests in property. I.R.C. § 2503(b); Treas. Reg. § 25.2503-3.

In addition, each spouse would be obligated to file a federal gift tax return with respect to his or her present interest gifts of individual property assets or of predetermination date property assets that alone or in combination with marital property assets exceed \$13,000 to any donee in any calendar year. It is with regard to gifts of individual property and predetermination date property assets, rather than marital property assets, that the gift-splitting provisions of I.R.C. § 2513 may be relevant.

Under I.R.C. § 2513, both spouses may signify their consent to treat all gifts made during the calendar year by one spouse to any person (other than the other spouse) as though made one-half by each spouse. For purposes of I.R.C. § 2513(a), a person is treated as the spouse of another person only if he or she is married to that individual at the time of the gift and does not remarry during the remainder of the calendar year. Spouses consenting to split gifts of individual property assets or of predetermination date property assets for any calendar year are jointly and severally liable for the entire amount of gift tax imposed on each spouse for that year. I.R.C. § 2513(d).

The election to gift split under I.R.C. § 2513 must be signified by both spouses on a federal gift tax return (Form 709). The mechanics are spelled out in Treasury Regulation § 25.2513-2. Normally the donor spouse should file such a return when the present interest gifts to any one donee of individual property assets and predetermination date property assets, either alone or in combination with marital property assets, exceed the \$13,000 annual gift tax exclusion in any calendar year, because if the present interest gifts to each donee are less than that amount, gift splitting would not be necessary. A return should also be filed when future interest gifts in any amount have been made. The consenting spouse must file a return only if his or her present interest gifts to any one donee (including deemed gifts by reason of that spouse's consent to gift split) will exceed the \$13,000 annual gift tax exclusion, or if future interest gifts are involved.

The personal representative of a deceased spouse, or the guardian of a legally incompetent spouse, may signify the consent to gift split. Treas.

Reg. § 25.2513-2(c). A limited right of revocation of the consent is provided under I.R.C. § 2513(c).

If a nondonor spouse files a federal gift tax return with respect to a gift of marital property assets made by the donor spouse, or consents to gift split on the donor spouse's federal gift tax return, he or she will probably be deemed to have "acted together" with the donor spouse in making a gift for Wisconsin property law purposes. See 1985 Trailer Bill Supplemental Nontax Note to section 766.53; see also *supra* § 9.86. If the donor spouse makes the gift to a third person, and both spouses file federal gift tax returns reporting their respective halves of the gift, they have probably acted together for purposes of section 766.53. If the donor spouse erroneously reports the entire amount of the gift on his or her own federal gift tax return, and the nondonor spouse signifies his or her consent to gift split under I.R.C. § 2513, this, too, should be sufficient evidence that the spouses acted together in making the gift.

## **P. Federal Gift Tax: Transfers Pursuant to Property Settlements [§ 9.100]**

The area of transfers in connection with releases or settlements of marital or property rights, whether before, during, or after marriage, has been fraught with gift tax hazards. In the context of the Act, these problems are likely to arise in conjunction with marital property agreements and divorce settlements.

As a general proposition, for purposes of I.R.C. § 2512(b), a release of property rights incident to marriage such as "dower or curtesy, or of a statutory estate created in lieu of dower or curtesy, or of other marital rights in the spouse's property or estate" is not considered "adequate and full consideration for money or money's worth" for any provision made for the relinquishing spouse by the other spouse. Treas. Reg. § 25.2512-8. Thus, property transfers in consideration of such releases have long been held to be subject to federal gift tax. *Commissioner v. Wemyss*, 324 U.S. 303 (1945); *Merrill v. Fahs*, 324 U.S. 308 (1945); Rev. Rul. 79-312, 1979-2 C.B. 29. This tax result follows whether the transfer pursuant to a marriage takes place before or after the marriage. The main difference, of course, is that since 1948, the federal gift tax marital deduction in I.R.C. § 2523, discussed in section 9.107, *infra*, potentially has been available to soften (or eliminate) the blow for gifts between spouses completed after the parties were actually married.

➤ **Note.** For gift tax purposes, the IRS has taken the position that support rights differ from marital rights, with the result that a spouse's release of support rights is sufficient consideration to bar gift tax to the extent of the value of those rights. Rev. Rul. 68-379, 1968-2 C.B. 414. This rule is relevant only in situations in which the support agreement does not fall within the time limitation of the special statute dealing with settlement agreements entered into incident to divorce. See I.R.C. § 2516.

Transfers in connection with divorce property settlement agreements historically also proved troublesome. Because of the availability of the federal gift tax marital deduction, the problem was not serious if the transfers could be carried out by the spouses before the entry of a divorce decree. Difficulties could and did occur after the entry of a divorce decree, because the federal gift tax marital deduction obviously was not available for transfers between former spouses. One alternative was to have the property transfers (whether or not made under an agreement) validated by incorporation in a final decree of a divorce court having the power to direct the disposition of the spouses' property, in which case the transfers would be considered judicially directed and not taxable gifts. *Harris v. Commissioner*, 340 U.S. 106 (1950). Further, a claim based on the decree would be deductible for federal estate tax purposes under I.R.C. § 2053 as a liquidated debt. Rev. Rul. 60-160, 1960-1 C.B. 374.

These problems led to the enactment of I.R.C. § 2516. This statute applies when a husband and wife enter into a written agreement relative to their marital and property rights, and divorce occurs within a three-year period beginning one year before the agreement was entered into. In such circumstances, any transfers of property or interests in property made under the agreement (1) to either spouse in settlement of his or her marital or property rights, or (2) to provide a reasonable support allowance for children of the marriage during their minority, are deemed to be transfers made for a full and adequate consideration in money or money's worth, regardless of whether the agreement is in fact approved by the divorce decree. Transfers that meet the I.R.C. § 2516 test with respect to transfers in settlement of marital or property rights will be deductible for federal estate tax purposes under I.R.C. §§ 2053(e) and 2043(b)(2). The procedures for specific disclosure of transfers coming within I.R.C. § 2516 are in Treasury Regulation § 25.6019-3(b). But see Technical Advice Memorandum 200011008 (Mar. 17, 2000), for an example of a transfer that did not qualify under I.R.C. § 2516; the IRS



held that payment of life insurance proceeds from a policy on the life of the divorced husband to adult children from the marriage was not made in settlement of marital or property rights for purposes of section 2516.

## **Q. Federal Gift and Estate Tax: Disclaimers [§ 9.101]**

### **1. In General [§ 9.102]**

The federal gift and estate tax rules with respect to disclaimers are spelled out in I.R.C. § 2518. The effect of making a *qualified disclaimer* for purposes of I.R.C. § 2518(a) is that the disclaimed interest in property is treated as though it had never been transferred to the disclaimant, thus avoiding all federal transfer taxation with respect to the disclaimer.

For a disclaimer to be qualified, and therefore not treated as a gift for federal gift tax purposes, it must comply with the requirements of I.R.C. § 2518 and the corresponding Treasury regulations. There are five basic requirements for a disclaimer to be qualified under I.R.C. § 2518: (1) it must be irrevocable and unqualified; (2) it must be in writing; (3) the writing must be delivered in a timely manner (generally within nine months of the event creating the property interest); (4) the disclaimant must not have accepted the interest disclaimed or any of its benefits; and (5) the interest disclaimed must pass without any direction on the part of the disclaimant. Treas. Reg. § 25.2518-2(a); *see also* Wis. Stat. § 854.13 (setting forth requirements for effective disclaimer in Wisconsin).

### **2. Marital Property Assets [§ 9.103]**

A surviving spouse may disclaim the deceased spouse's marital property interest that passes to him or her, provided that an acceptance of the benefits of the disclaimed property is avoided. *See* Treas. Reg. § 25.2518-2(c)(5), Example (11). A disclaimer of the decedent's community property interest in a residence will not by itself be barred by the survivor's occupancy of the residence following death. Treas. Reg. § 25.2518-2(d)(4), Example (8). A surviving spouse, however, cannot disclaim his or her own one-half interest in marital property assets, if only because the surviving spouse is the transferor of his or her own one-half interest. *See* Rev. Rul. 83-35, 1983-1 C.B. 234; Treas. Reg. § 25.2518-2(c)(5), Example (10). It follows that an attempted disclaimer of both halves of a marital property asset by a surviving spouse after the

death of the first spouse, coupled with a transfer of the disclaimed asset to the person who would otherwise be entitled to receive the property, will constitute a gift by the survivor of his or her own one-half marital property interest.

In Private Letter Ruling 8624103 (Mar. 19, 1986), the IRS confirmed that the surviving spouse may execute a partial disclaimer of the decedent's community property interest in real estate without causing a taxable gift. The disclaimer was structured to disclaim an undivided interest in the real estate equal in value to the largest amount that could pass free of federal estate tax by reason of the unified credit and the credit for state death taxes.

### **3. Individual Property and Predetermination Date Property Assets [§ 9.104]**

Does Wisconsin's statutory rule classifying the income from individual property assets and predetermination date property assets as marital property raise a question as to whether the spouse making a disclaimer of such property at death has already accepted its benefits during the marriage, thus causing the disclaimer to be nonqualified? Based on a private letter ruling issued by the IRS, the answer appears to be no. Specifically, in Private Letter Ruling 8212061 (Dec. 24, 1981), the IRS indicated that the presence of a community property interest in income from property during the marriage will not preclude a timely disclaimer by the surviving spouse upon the death of his or her spouse when the actual transfer of the property interest to the disclaimant did not occur until death.

The private letter ruling involved disclaimer of a contingent future income interest in a trust in Texas, which has an income rule similar to that in Wisconsin. During her marriage, the wife established an irrevocable trust, which reserved an income interest to her for life and provided for payment of income to her husband following her death unless she exercised a limited power of appointment to direct the trust assets to her issue. The wife and husband were later divorced, but the husband nevertheless remained a cotrustee. The wife died without having exercised the limited power of appointment, and under Treasury Regulation § 25.2511-2, the transfer of the interests in trust became complete. Under the laws of Texas, the husband had a community property interest in the wife's income from the trust during the period of

their marriage. The IRS determined that this interest did not give rise to an acceptance that later would bar the husband's disclaimer of his contingent successor income interest following the wife's death. The IRS further pointed out that acceptance could not become an issue until the wife's death, when the transfers of trust interests were deemed to be completed. Priv. Ltr. Rul. 8212061 (Dec. 24, 1981).

The result in Private Letter Ruling 8212061 is consistent with the analysis in *Estate of Wylie*, 610 F.2d 1282, discussed in section 9.62, *supra*. There should be no deemed acceptance of benefits from individual or predetermination date property assets by the surviving spouse solely because of the preexisting statutory right to a marital property interest in the income from the property. The right to a share of income arises by operation of law and requires no action on the part of the surviving spouse, unlike the typical case involving acceptance of benefits from a lifetime gift or a testamentary disposition. Moreover, the right to a share of income is totally terminable by the owner of the property during lifetime through execution of a unilateral statement, gifts to third parties, or reinvestment in nonincome-producing assets. These factors underscore the conclusions that there is likely to be no "acceptance" in the usual sense, as well as that the "benefits" during the owner spouse's lifetime are insubstantial, if not illusory.

#### **4. Survivorship Marital Property Assets [§ 9.105]**

For Wisconsin property law purposes, survivorship marital property is indistinguishable from other kinds of marital property during the joint lifetimes of the spouses; it is merely a form of holding marital property. *See* Wis. Stat. § 766.60(5)(a); *see also supra* § 2.250. Upon the death of one of the spouses, however, the ownership rights of the deceased spouse in the property vest solely in the surviving spouse by a nontestamentary disposition at death. *Id.*

As discussed in section 9.30, *supra*, the characteristics of survivorship marital property bear little resemblance to those of joint tenancy with right of survivorship other than the feature of survivorship. Each of the two joint tenants owns an equal interest *in the whole property* for the duration of the tenancy, and upon the death of one of the two, the interest of the deceased disappears and the survivor becomes the sole owner of the whole. *See* Wis. Stat. § 700.17(2). In contrast, the ownership interest of each spouse in assets classified as survivorship marital

property consists of a present undivided one-half interest in the property. Wis. Stat. § 766.31(3). When title to an asset is held as survivorship marital property, on the death of a spouse, the deceased spouse's undivided one-half ownership interest vests solely in the surviving spouse by a nontestamentary, nonprobate transfer. Wis. Stat. § 766.60(5). Moreover, a spouse's interest in a joint tenancy may be unilaterally severed and the right of survivorship destroyed during his or her lifetime, whereas this ordinarily cannot be done with survivorship marital property without action by both spouses.

For purposes of disclaimers under I.R.C. § 2518, a deceased spouse's interest in survivorship marital property assets should be regarded the same as any other marital property interest, and should be subject to disclaimer in the same manner and on the same conditions as marital property assets. *See supra* § 9.103. By statute, Wisconsin specifically authorizes a surviving spouse to disclaim the decedent spouse's interest in survivorship marital property. Wis. Stat. § 701.26(1)(b).

The regulations under I.R.C. § 2518 regarding the disclaimer of joint interests alleviate any possible concern that may exist with respect to the time period for making a qualified disclaimer of survivorship marital property. Although the regulations do not specifically mention survivorship marital property (or its analogue, community property with rights of survivorship), they do confirm the timing issue with respect to disclaiming the survivorship interest in jointly owned property that is not unilaterally severable.

Before the adoption of the regulations in 1997, the IRS had taken the position in a number of rulings that the time period for making a qualified disclaimer of a survivorship interest that was not unilaterally severable commenced upon creation of the tenancy and not at the decedent's later death. *See, e.g.*, Tech. Adv. Mem. 9208003 (Feb. 21, 1992) (involving Arkansas tenancy by entirety property); Tech. Adv. Mem. 9427003 (July 8, 1994) (involving Maryland tenancy by entirety property). The fact that survivorship marital property (like tenancy by the entirety property) is not unilaterally severable created concerns regarding the ability of a surviving spouse to disclaim a deceased spouse's interest in survivorship marital property upon the death of the first spouse.

These concerns were to put to rest, however, with the adoption of Treasury Regulation § 25.2518-2(c)(4)(i), which provides in pertinent part that

[a] qualified disclaimer of a survivorship interest to which the survivor succeeds by operation of law upon the death of the first joint tenant to die must be made no later than 9 months after the death of the first joint tenant to die regardless of whether such interest can be unilaterally severed under local law....

Example 8 under Treasury Regulation § 25.2518-2(c)(5) extends this application to tenancy-by-the-entirety property. The same rationale should also apply to a disclaimer by a surviving spouse of the deceased spouse's interest in survivorship marital property.

The disclaimer regulations also address the timing and extent to which a surviving spouse or other co-owner of a joint bank, brokerage, or other investment account may make a qualified disclaimer of a deceased spouse's interest. Under the regulations, if a surviving joint owner wishes to disclaim contributions to an account made by a deceased co-owner, the disclaimer must be made within nine months of the deceased co-owner's death and the surviving co-owner may not disclaim any portion of the joint account attributable to consideration furnished by the surviving co-owner. Treas. Reg. § 25.2518-2(c)(4)(iii). Of course, if the property in the account were classified as marital property, then the disclaimer would be limited to one-half of the value of the account at the death of the deceased spouse.

## **5. Marital Property Assets Transferred by Survivorship Will Substitute Agreement [§ 9.106]**

The regulations under I.R.C. § 2518 do not contemplate the timing or extent to which a disclaimer may be made with respect to property passing under a will substitute agreement as authorized by Wis. Stat. § 766.58(3)(f) (or by the similar laws of the state of Washington). In Private Letter Ruling 9507017 (Feb. 17, 1995), however, the IRS considered a disclaimer with respect to property passing to the surviving spouse under a Washington community property agreement and concluded that “for purposes of section 2518(a)(2), the nine-month period for making the disclaimer of the decedent's one-half community property interest passing to surviving spouse under the community

property agreement commences on the date of death.” Similarly, it would seem clear that the time period for the making of a disclaimer by a Wisconsin surviving spouse of property passing under a will substitute agreement pursuant to section 766.58(3)(f) should commence upon the date of death of the first spouse to die.

## **R. Federal Gift Tax: Marital Deduction [§ 9.107]**

### **1. Gifts Between Spouses [§ 9.108]**

The gift tax marital deduction in I.R.C. § 2523 roughly parallels the federal estate tax marital deduction in language and in practice. An unlimited deduction is allowed to a donor for all gifts made during the calendar year to a donee who, at the time of the gift, is the donor’s spouse. I.R.C. § 2523(a). With certain exceptions, gifts of terminable interests in property do not qualify for this deduction. I.R.C. § 2523(b); Treas. Reg. § 25.2523(b)-1. The exceptions are for certain types of deductible terminable interests described in Treasury Regulation §§ 25.2523(d)-1 (joint interests) and 25.2523(e)-1 (life estate with power of appointment).

In rearranging or revising family estate plans, spouses may transfer property or property interests. Transfers also may occur either when one spouse makes additions or improvements to marital property assets with his or her individual property funds or when one spouse makes improvements to the individual property assets of the other spouse with marital property funds. While most of these transfers will involve entire properties or interests in property, it is possible that arrangements will be established that do not qualify for the federal gift tax marital deduction.

➤ **Caution.** It must be remembered that the federal marital deduction provision in I.R.C. § 2523 is not a blanket exemption of transfers to a spouse. Care should be exercised in making sure that transfers to a spouse are of a nature that qualifies for the marital deduction. If there are any future interest gifts or transfers to a spouse that do not qualify for the gift tax marital deduction, then a gift tax return must be filed.

## 2. Special Rules for Gifts to a Spouse Who Is Not a United States Citizen [§ 9.109]

Under I.R.C. § 2056(d), the estate tax marital deduction for transfers of property interests to a surviving spouse who is not a citizen of the United States is effectively denied unless the property passes to the surviving spouse in a qualified domestic trust. Attributes of a qualified domestic trust are described in detail in I.R.C. § 2056A.

A parallel provision under I.R.C. § 2523(i) disallows the gift tax marital deduction for lifetime transfers to noncitizen spouses. However, I.R.C. § 2523(i)(2) creates a special rule to generate the equivalent of a \$100,000 annual exclusion for gifts to a noncitizen spouse, provided that the gift would otherwise qualify for the federal gift tax marital deduction. Since 1998, the \$100,000 annual exclusion for gifts to a noncitizen spouse has been indexed for inflation. For 2010, the amount is \$134,000. Rev. Proc. 2009-50, 2009-45 I.R.C. 617.

If spouses domiciled in Wisconsin are contemplating the execution of an opt-in marital property agreement of the type described at sections 7.151 or 7.175, *supra*, and the noncitizen spouse has substantially fewer assets than the other spouse, caution must be exercised to avoid creating a major taxable gift when the opt-in agreement is executed. For example, if the citizen spouse owns individual property or predetermination date property assets valued at \$1 million before execution of the marital property agreement and the noncitizen spouse owns similar assets with a value of \$100,000, the execution of an agreement classifying all or substantially all of the spouses' property as marital property will result in a gift to the noncitizen spouse of \$450,000 ( $\$1,000,000/2 - \$100,000/2 = \$450,000$ ). Under I.R.C. § 2523(i), the amount of such gift in excess of the then annual exclusion amount would be treated as a taxable gift subject to federal gift tax. Thus, executing a marital property agreement may trigger either an immediate gift tax liability or possibly require the use of a substantial portion of the donor spouse's \$1 million lifetime gift tax exemption that was intended to shelter transfers to the donor's children or other family members.

➤ **Note.** This gift tax problem apparently does not occur when the noncitizen spouse passively becomes the owner, by operation of law, of an undivided one-half community property interest in property because he or she resides in a community property jurisdiction. *See*,

*e.g.*, Rev. Rul. 74-284, 1974-1 C.B. 276; *see also Fernandez v. Wiener*, 326 U.S. 340 (1945).

#### **IV. Wisconsin Transfer Taxes [§ 9.110]**

As discussed in section 9.55, *supra*, in 2001 Congress passed the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, 115 Stat. 38 (“the 2001 Act”), which made extensive changes to the federal estate and gift tax regime, including a reduction in estate tax rates and a substantial incremental increase in the federal estate tax exemption. Standing alone, the increase in the federal estate tax exemption would have meant declining estate tax revenue to Wisconsin and other states with a pick-up estate tax system which imposes a state estate tax equal to the maximum state death credit allowed for federal estate tax purposes.

In response to the 2001 Act’s reduction and scheduled repeal of the state death tax credit, Wisconsin revised its estate tax law to provide that, effective October 1, 2002, the federal state death tax credit and the federal estate tax exemption to be used for purposes of determining Wisconsin estate taxes for deaths occurring from October 1, 2002 through December 31, 2007, must be computed under the federal estate tax law in effect on December 31, 2000. The federal state death tax credit and the federal estate tax to be used for purposes of determining Wisconsin estate tax for deaths occurring after December 31, 2007 must be computed under the federal estate tax law in effect on the date of the decedent’s death. Wis. Stat. § 72.01(11m), (11n). Accordingly, under current law, the imposition of a Wisconsin estate tax will be dependent upon the status of the federal estate tax.

Historically, there have been no special provisions contained in the Wisconsin estate tax law to accommodate the Act or the system of community property ownership it creates. No such provisions have been necessary because Wisconsin’s estate tax, since the enactment of the Act, has been imposed upon property that is subject to the federal estate tax. The application of the Act’s system of community property will presumably continue to be interpreted consistently with federal estate tax law principles under any future version of the Wisconsin estate tax that may be enacted.



# Marital Property Law in Wisconsin

Fourth Edition

Volume III

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## Note to Readers

# 10

## Estate Planning

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The authors have determined that the uncertain status of the laws concerning the estate and generation-skipping transfer taxes necessitated holding off on comprehensively revising this chapter. The book's editors made stylistic changes to the chapter but did not make substantive changes. The following is a brief summary of the current status of estate and transfer taxes.

### ***The Temporary “Repeal” and Uncertain Future of the Federal Estate and Generation-skipping Taxes***

In 2001, a federal law (the Economic Growth and Tax Reconciliation Act of 2001 [hereinafter 2001 Tax Act]) was adopted that made significant changes to the federal estate and generation-skipping transfer (GST) tax laws. The 2001 Tax Act contained a provision for the “repeal” of the estate and GST taxes in 2010 and a “sunset” of the 2001 Tax Act at the end of 2010. Although the clear expectation was that the 2001 Tax Act would be revisited before the one-year repeal in 2010, Congress has not yet acted.

Thus, as of publication of this revision to *Marital Property Law in Wisconsin*, federal estate and GST taxes do not apply with respect to deaths that occur in 2010 or generation-skipping transfers made in 2010. The federal gift tax, which applies to gifts made during life, remains in effect (with some modifications). Along with the repeal of the estate and GST taxes comes a new rule regarding carry-over basis for capital assets. This new rule differs from the basis-adjustment rule—commonly referred to as *stepped-up basis*—that applies when the estate tax is applicable. The new carry-over basis rules are complex. Generally, however, the new rules allow allocation of \$1.3 million of basis

adjustment to assets passing to anyone and an additional \$3 million of basis adjustment to assets passing to or for the direct benefit of a surviving spouse.

Under current law, the repeal of the federal estate and GST taxes is scheduled to last for just one year, and the estate and GST taxes are scheduled to be reinstated on January 1, 2011, but with significant differences from the law as it existed in 2009. The most notable difference is a return to an estate tax exemption of only \$1 million per person instead of the \$3.5 million exemption that applied in 2009. Adding to the complexity is the possibility that Congress will reinstate or revise the estate and GST taxes and try to make those changes retroactive to January 1, 2010.

This state of affairs creates potential opportunities and considerable uncertainty for many existing estate plans. Estate plans most likely to be affected are those that include formula provisions tied to (1) the federal estate tax marital deduction/exclusion amount, (2) the federal estate tax charitable deduction, or (3) the federal GST tax exemption. Other plans may be affected as well, depending on the makeup of assets and their intended disposition.

### ***Federal Gift Tax Law***

The 2001 Tax Act limited the lifetime exemption from the federal gift tax to \$1 million per donor, with any use of the lifetime exemption to be charged against the federal estate tax exemption (which, as noted above, is scheduled to return in 2011). The 2001 Tax Act also reduced the gift tax rate to 35% for gifts made in 2010 (although, as in the case of the estate and GST taxes, Congress might try to enact a law changing that retroactively).

The lifetime exemption is consumed only in the case of “taxable gifts.” Taxable gifts do not include gifts of a so-called present interest that are within the gift tax annual exclusion amount (in 2010, \$13,000 per donor for an unlimited number of donees). Taxable gifts also do not include direct payments (in any amount) for another person’s qualified tuition or medical expenses as long as the payments are made directly to the school or medical provider.

### ***Wisconsin Estate Tax***

The former Wisconsin estate tax expired at the end of 2007. Under current law, for Wisconsin residents dying after 2007, there is no Wisconsin estate tax for assets that have a taxable situs in Wisconsin. It is of course possible that the state law on estate taxes (as with any law) could change. For now, however, Wisconsin does not have an estate tax, nor does it have a gift tax or GST tax. (For persons who own property in a state that still has an estate or inheritance tax, state death taxes still can be an issue.)

### ***Marital Property Agreements***

In the case of married persons who plan their estates together, a marital property agreement often is an integral part of the estate plan. Marital property in Wisconsin is a form of community property, which has a unique tax attribute: upon the death of one spouse when the estate tax is applicable, both halves of a marital property asset receive an adjustment in basis. While sometimes this double adjustment in basis results in a double step-up, it could instead result in a double step-down if the value of the asset has fallen below its income tax basis.





## Estate Planning

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## **I. Scope of Chapter [§ 10.1]**

This chapter assumes a fundamental knowledge of law and practice relating to estate planning. Its focus is on the marital property law implications of estate planning in Wisconsin. The classification and ownership rules under marital property law have significant implications both for property disposition (lifetime as well as death transfers) and taxation (income as well as transfer taxes). In addition, the marital property law may have significant implications with respect to creditors' rights in certain situations. This chapter addresses these and other issues the estate planner must consider when advising married persons in Wisconsin.<sup>1</sup>

For a discussion of income and transfer tax issues relating to marital property, see chapter 9, *supra*. For a discussion of estate planning generally, see John R. Price, *Price on Contemporary Estate Planning* (2d ed. 2000 & Supp.); Susan Collins et al., *Eckhardt's Workbook for Wisconsin Estate Planners* (State Bar of Wisconsin CLE Books 5th ed. 2008).

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2005–06 Wisconsin Statutes, as affected by acts through 2007 Wisconsin Act 19. Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”



## **II. Separate vs. Joint Representation [§ 10.2]**

In most cases, spouses will work together in developing an integrated estate plan based on common goals and objectives and will retain the same counsel in a joint representation relationship. In such instances, it is advisable for counsel to have his or her clients sign a joint (or dual) representation letter after consultation. See chapter 14, *infra*, for a discussion of representation of spouses jointly in estate planning. Sometimes, however, counsel may be advising only one spouse, whose objective may be to minimize the impact the marital property law has on the other spouse's ability to assert property rights. In either case, marital property law and its impact from both a property law and tax law standpoint should be considered, including the impact on the rights of creditors and division of property in the event of dissolution of the marriage.

## **III. Basic Estate Planning Considerations Under Marital Property Law [§ 10.3]**

### **A. Marital Property Fundamentals [§ 10.4]**

#### **1. Application of Chapter 766 to Spouses [§ 10.5]**

Wisconsin's marital property law has a pervasive effect on the property rights of spouses in Wisconsin. As a result, when marital property law applies, it is important to consider its implications for the estate plan.

Chapter 766 specifies when that chapter begins to apply to spouses and when it ceases to apply. See Wis. Stat. § 766.03. Both spouses must be domiciled in Wisconsin for the marital property law to apply to property rights acquired by the spouses. Wis. Stat. §§ 766.01(8), .03(1). Even if both spouses are domiciled in Wisconsin, the marital property law does not purport to classify certain assets acquired before the determination date (*predetermination date property*), such as property acquired before 1986 or property acquired before the spouses became domiciled in Wisconsin (but the law may nonetheless confer elective rights as to such property at the death of the first spouse). And even when chapter 766 no longer applies to spouses, property rights acquired and obligations incurred while the law applied continue. Wis. Stat.

§ 766.03(3). For spouses moving from Wisconsin (or if only one spouse moves from Wisconsin), the preservation of marital property rights acquired while chapter 766 applied may be an important tax-planning consideration.

➤ **Note.** Before the amendment of chapter 766 by 1987 Wisconsin Act 393 [hereinafter 1988 Trailer Bill], application of chapter 766 was dependent on the spouses' having a "marital domicile" in Wisconsin. The reference to marital domicile was eliminated because of the uncertainty concerning its meaning.

## **2. Classifications and Presumptions [§ 10.6]**

Under the marital property law, all property of spouses is classified as marital property unless classified otherwise under chapter 766 or unless not classified by reason of having been acquired before the spouses' determination date. Wis. Stat. § 766.31. All property acquired by spouses is presumed to be marital property. Wis. Stat. § 766.31(2). Subsections 766.31(6) and (7) identify property classified as individual property. Establishing that property is not marital property generally requires proof of the time, method, or source of acquisition in a manner that shows that the general classification as marital property should not apply. For a general discussion of classification of property, see chapter 2, *supra*. For a discussion of the classification of property when mixing has occurred, see chapter 3, *supra*.

## **3. Spouses' Respective Interests in Marital Property Assets [§ 10.7]**

Each spouse owns a present undivided one-half interest in each marital property asset. Wis. Stat. § 766.31(3). That interest continues throughout the marriage unless the asset is reclassified by one of the means specified under the marital property law. Each spouse's ability to deal with a marital property asset during the ongoing marriage is affected by rules relating to management and control under section 766.51, the remedies for gifts of marital property in excess of the limits specified under section 766.53, the duty of good faith under section 766.15, and the remedies afforded under section 766.70.

#### **4. Respective Interests of Surviving Spouse and Successor in Interest to Deceased Spouse in Former Marital Property Assets [§ 10.8]**

Upon the death of a spouse, the surviving spouse retains his or her undivided one-half interest in each item of marital property regardless of title. Wis. Stat. § 861.01. The surviving spouse's interest is not subject to administration, and a third party who is a successor in interest to all or part of the decedent's one-half interest (such as the decedent's personal representative) is a tenant in common with the surviving spouse. *Id.*

#### **5. Spouses' Ability to Reclassify by Marital Property Agreement and Other Methods [§ 10.9]**

Chapter 766 gives spouses considerable flexibility to modify the property regime otherwise specified by statute. Section 766.17(1) provides that, with limited exceptions, spouses may vary the effect of chapter 766 by marital property agreement. A marital property agreement may classify assets in a different manner than the law would otherwise specify. Assets may be classified or reclassified by other means as well, as specified in section 766.31(10), or by taking title in certain forms, Wis. Stat. § 766.60. Thus, a spouse who owns an individual property asset or predetermination date property asset may reclassify it as marital property. Spouses may reclassify a marital property asset as the individual property of one spouse. This flexibility to alter property rights can be an important part of achieving the spouses' estate planning objectives. For a discussion of marital property agreements, see generally chapter 7, *supra*. For a discussion of considerations involved in deciding whether to reclassify assets and determining the method of reclassification, see sections 10.18–.33, *infra*.

Spouses can also unintentionally reclassify assets—for example, by mixing marital and nonmarital property assets or by applying efforts to the improvement of nonmarital property assets. For a discussion of reclassification by way of such mixing, see chapter 3, *supra*. Unintentional reclassification also can occur by taking title to assets in certain joint forms (for example, taking title as “tenants in common” or “joint tenants”). See Wis. Stat. § 766.60(4)(b). From a planning standpoint, spouses need to understand the potential effects of their

actions to avoid unanticipated reclassification that may undermine aspects of their estate planning.

## **6. Item-by-item Rule [§ 10.10]**

The difference between the item-by-item rule and the aggregate rule is a significant marital property concept. Wisconsin follows the item-by-item rule. Wis. Stat. § 861.01.

Under the *aggregate rule*, at the death of one spouse, the surviving spouse owns one-half the community property assets in the aggregate, not in each and every item. For example, if the aggregate community property assets are \$100,000 and one spouse dies, the surviving spouse owns \$50,000 but does not have an ownership interest in each and every asset. In contrast, under Wisconsin's *item-by-item rule*, the surviving spouse owns an undivided one-half interest in each and every former marital property asset, as a tenant in common. Wis. Stat. § 861.01.

The item-by-item rule is important for several reasons. As part of the estate planning process, the assets that can be disposed of by each spouse must be ascertained. A marital property agreement may be necessary so that one spouse is able to dispose of a particular asset. If a spouse wishes to dispose of an entire asset but owns only one-half of it, participation of the other spouse is necessary to make a complete and final disposition of the asset. This participation can be accomplished by various means but is often accomplished with a marital property agreement. Conversely, the spouses must be careful not to make unanticipated dispositions. For example, a general residuary clause in the deceased spouse's will may result in an unanticipated transfer of a one-half interest in those assets if a third party is the beneficiary of the residuary clause.

2005 Wisconsin Act 216, section 42, created section 766.31(3)(b) to permit distribution on an aggregate rather than on an item-by-item basis so as to allow more flexibility in the administration of the estate of the first deceased spouse. For a general discussion of this provision, see section 2.22, *supra*. For a discussion of the federal and Wisconsin tax issues relative to this change, see section 9.20, *supra*. For suggested provisions to include in a marital property agreement to accommodate this change, see section 7.151, *supra*.

## **7. Title vs. Ownership [§ 10.11]**

Under Wisconsin's previous common law system, title and ownership were largely synonymous. If one spouse were the sole grantee on the deed to a parcel of real estate, that spouse was the sole owner of the real estate. Title and ownership are not synonymous under Wisconsin's marital property law. For example, one spouse may be the sole grantee of the residence, but the residence may be marital property, so that each spouse has a vested, one-half ownership interest in the residence. The concept that one can be an owner and not be a titleholder is significant; it is this concept that causes the most difficulty in applying the marital property law.

As a result of the potential difference in title and ownership, the estate planner gathering information from married clients may need to ask more than simply which spouse holds title to an asset. *How* the asset was acquired, *when* it was acquired, and with *what* it was acquired also are potentially significant questions in ascertaining ownership of the asset.

## **8. Management and Control [§ 10.12]**

Under Wisconsin's previous common law system, ownership was largely synonymous with management and control. For example, if stock were titled in one spouse's name alone, that spouse had the sole right to manage and control the stock. But under Wisconsin's marital property system, ownership is not synonymous with management and control. Generally, title, not ownership, determines the right to manage and control. Thus, if stock classified as marital property is registered in one spouse's name alone, that spouse has the right to manage and control the stock, even though the spouse has only a one-half ownership interest. Conversely, the other spouse has no right of management and control despite being a one-half owner of the stock.

## **9. Gifts and Remedies [§ 10.13]**

Lifetime gifts may be an integral part of the estate plan. If the subject of a gift is a nonmarital property asset (e.g., individual property or predetermination date property), the married donor need not be concerned about property rights and tax consequences arising from the marital property law, with one exception. If predetermination date

property assets that meet the definition of *deferred marital property* are given away within two years of the donor's death or if the donor transfers such property while retaining certain rights in the transferred property, the assets may be included within the deferred marital property election available to the surviving spouse and may be subject to recovery. *See* Wis. Stat. §§ 861.03(3), (4), .06(4).

When a marital property asset is the subject of a gift, the gift will be deemed for federal gift tax purposes to have been made by both spouses, even if one spouse acted alone in making the gift. This may facilitate the efficient use of gift and generation-skipping transfer (GST) tax annual exclusions, applicable credit amounts, and GST exemptions. A gift-splitting election is not necessary when the subject of the gift is a marital property asset. The treatment of the gift as having been made one-half by each spouse also may give rise to unanticipated estate tax consequences. *See* chapter 9, *supra*, for a general discussion of the tax consequences of gift transactions.

The right to manage and control a marital property asset includes the power to make a gift of that asset to a third party, but a gift that exceeds the limit specified by section 766.53 gives rise to a right of recovery by the other spouse unless the spouses acted together in making the gift. Wis. Stat. §§ 766.53, .70(6)(a). From a planning standpoint, if the spouses jointly intend to make a gift of a marital property asset to a third party, contemporaneous evidence of both spouses' intent may eliminate questions that could arise later. For example, if a spouse having management and control of a marital property asset makes a gift of that asset (in excess of the section 766.53 limit) to a trust and the other spouse subsequently dies without having evidenced an intent to join in the gift, the personal representative of the deceased spouse may feel compelled to pursue the remedy provided under section 766.70(6)(a). A contemporaneous written consent by the spouse not having management and control could eliminate uncertainty.

## **10. Nonseverability of Marital Property Assets**

### **[§ 10.14]**

Each spouse owns a present undivided one-half interest in a marital property asset. Wis. Stat. § 766.31(3). Spouses can reclassify an asset as marital property, but a marital property asset cannot be severed by the spouses. If a marital property asset is divided in two parts, each part

remains marital property. If the spouses wish to divide a marital property asset, so that each spouse is the sole owner of a portion, the spouses must reclassify the asset as individual property. This reclassification can be accomplished before or after a division has occurred. With regard to the prohibition against unilateral severance of marital property assets, see section 2.23, *supra*.

## **11. Taxation [§ 10.15]**

The Internal Revenue Service (IRS) has recognized that marital property under chapter 766 is a form of community property. Rev. Rul. 87-13, 1987-1 C.B. 20. This is significant because there is an established body of federal tax law concerning income and transfer taxes as they relate to community property assets. Chapter 9, *supra*, discusses principles of income and transfer taxation and the application of those principles to marital property assets.

### **B. Deferred Marital Property Elective Rights [§ 10.16]**

The comprehensive revision of the probate code under 1997 Wisconsin Act 188, which took effect on January 1, 1999, included a wholesale revision of the former deferred marital property election against probate assets and the augmented marital property estate election against nonprobate assets. The former elections have been combined into a single deferred marital property election under section 861.02, which applies to both probate and nonprobate assets and provides for a pecuniary amount rather than an item-by-item election.

From a planning perspective, the assertion of the deferred marital property election has the effect of altering the plan of disposition that otherwise would apply at the death of the first spouse. When spouses have planned together under circumstances in which they are represented by the same counsel and have put in place a plan that reflects shared goals and objectives, the possible existence of elective rights is generally of little consequence. Indeed, in most of these situations, the spouses will have entered into a comprehensive marital property agreement that classifies their assets either as marital property or individual property so that there is no election to be made.

But when spouses are not working together in their estate planning, the existence of the deferred marital property election is something for each to consider. If the spouses have previously entered into a marital property agreement defining their respective rights and obligations, the agreement will normally include a waiver of spousal elective rights. In such a situation, the estate planning that follows need not take into account elective rights (unless there is concern about the enforceability of the marital property agreement). In situations in which there is no marital property agreement or in which there is concern about the enforceability of a marital property agreement, the extent to which the exercise of the deferred marital property elective right could upset a plan of disposition should be considered. For a discussion of alternatives for limiting the impact of elective rights at death, see section 10.169, *infra*.

### **C. Intestacy [§ 10.17]**

A thorough estate plan normally will result in no assets passing by way of intestacy. However, the estate planner should be aware of the manner in which assets would devolve in the absence of effective provisions in a will. The rules of intestacy in the case of a deceased spouse are set forth in section 852.01.

## **IV. Classifying and Reclassifying Assets [§ 10.18]**

### **A. Determining Classification of Existing Assets of Spouses [§ 10.19]**

At the beginning of the estate planning process, the estate planner gathers information from the spouses that will be important to the estate plan, such as family information and information regarding assets and liabilities. From the perspective of marital property law, this information should include when the spouses were married, when they established their domicile in Wisconsin, and whether they have entered into any marital property agreements. The responses to all these inquiries may have implications concerning the classification of assets. Information gathered regarding assets and liabilities typically will include identification of the type of asset and how it is titled (in one spouse's name or in both names). Under a common law property regime, that information may be enough. In planning under the marital property law,



for some clients, it may be necessary to obtain further information to ascertain the classification of assets. For example, if an asset held in one spouse's name alone was acquired by gift or transfer at death, that asset will not be classified as marital property. Wis. Stat. § 766.31(7)(a), (8). The reclassification of the asset as marital property would have an effect on the owner's property rights, both during the ongoing marriage and at the termination of the marriage by death or dissolution. Hence, depending on the type of plan to be adopted, the estate planner may need to have spouses identify property that was acquired by gift or by transfer at death in the information-gathering process.

Similarly, the planner may wish to seek information regarding *when* an asset was acquired to ascertain whether it was acquired before or after the spouses' determination date. For example, publicly traded stock titled in the spouses' names as joint tenants that was acquired by them before 1986 is classified as joint tenancy property. *See* Wis. Stat. § 700.19. By contrast, publicly traded stock acquired by Wisconsin-domiciled spouses in their names as joint tenants after 1985 is survivorship marital property (with limited exceptions). *See* Wis. Stat. § 766.60(4)(b)1.a.; *supra* ch. 2.

Depending on the type of plan to be adopted, it may or may not be necessary to identify the classification of each and every asset owned by the spouses. In each instance, the planner must exercise judgment regarding what information is important to the estate plan.

## **B. Determining Whether Reclassification of Assets Is Appropriate for Spouses [§ 10.20]**

### **1. In General [§ 10.21]**

Under the marital property law, spouses have considerable flexibility in determining how assets are classified. As a result of the unlimited gift tax marital deduction, assets generally can be reclassified by spouses without any gift tax consequences, though caution should be observed in adopting any contractual provisions that might cause a donee spouse's interest to be deemed a gift of a nonqualified terminable interest. Further, caution should be observed if both spouses are not U.S. citizens, *see infra* § 10.131. Whether assets should be reclassified in each instance requires an exercise of judgment regarding whether the

reclassification will help achieve particular tax or nontax objectives. If the spouses decide to reclassify an asset, there is the further question of the method to use in achieving the reclassification (e.g., gift, conveyance, marital property agreement, written consent).

## **2. Preservation of Property Rights of Spouses**

### **[§ 10.22]**

The reclassification of an individual property asset as a marital property asset (or vice versa) changes each spouse's property rights regarding that asset. These may be rights during the marriage (e.g., rights with respect to management and control or the availability of the asset to satisfy the claims of certain creditors), rights at the death of a spouse (e.g., the right to dispose of all or part of the asset by will), or rights at dissolution of the marriage (e.g., the right to treat an inherited asset as not subject to property division). When spouses are working together in the estate planning process, the adjustment of their relative property rights may be in furtherance of shared goals and objectives (e.g., in the case of reclassification as marital property, the ability of the survivor to enjoy the tax benefits of a full adjustment in tax basis).

However, shared goals and objectives can change over time and sometimes diverge, or unforeseen circumstances can arise. The husband's inherited asset that has been reclassified as the marital property of both spouses may become the subject of property division at dissolution. The wife's former individual or predetermination date property asset reclassified as marital property can be reached by the husband's creditors to satisfy family-purpose obligations. Classification decisions are made in light of shared goals and objectives and possible or unforeseen circumstances. The estate planner should discuss with his or her clients the relative advantages and disadvantages of reclassifying assets in one manner or another.

## **3. Creating Certainty Regarding Classification of Assets**

### **[§ 10.23]**

As discussed at section 10.10, *supra*, Wisconsin's community property regime depends on an item-by-item classification of assets. This means that, at the death of one spouse, it is necessary to determine

the classification of each asset owned by the spouses. In some situations, this may not be difficult or may not be critical. For example, if the spouses were married after 1986, have been domiciled in Wisconsin during their entire marriage, and have acquired all of their assets through the expenditure of their efforts, determining the classification of assets may be a rather straightforward task. Similarly, if the estate plan provides that all assets are to pass to the surviving spouse, the precise determination of the classification of each and every asset may not be particularly significant.

In many situations, however, determining the classification of all the spouses' assets can be a daunting task, particularly in view of the general mixing and tracing rules under section 766.63 and the special classification rules for life insurance and deferred employment benefits under sections 766.61 and 766.62, respectively. But if the spouses have entered into a comprehensive marital property agreement during their lifetime, the determination of the classification of assets can be simplified immensely. Hence, a marital property agreement can add a level of certainty to the planning process and ultimately to the administration of the estate of the first spouse to die.

See section 10.10, *supra*, describing the option of deviating from the item-by-item rule by virtue of the change made to section 766.31(3) by 2005 Wisconsin Act 216, section 42.

#### **4. Utilization of Applicable Credit Amount (Unified Credit) or GST Exemption of Each Spouse**

**[§ 10.24]**

Efficient planning for the utilization of each spouse's applicable credit amount (unified credit) for federal estate tax purposes and, when applicable, each spouse's exemption from the federal GST tax (GST exemption) depends on each spouse having sufficient assets to dispose of at death to utilize the exclusion or exemption. Often, one spouse has more assets than the other spouse, which, if the spouse with fewer assets dies first, can undermine effective estate and GST tax planning.

➤ **Example.** If a husband has individual property or predetermination date property assets of \$2 million and his wife has individual property or predetermination date property assets of

\$600,000, the husband dies first, and the estate plan includes an optimal marital deduction/credit shelter plan, there would be no federal estate tax in the survivor's estate. If his death occurred in 2005 (when the federal estate tax exemption amount was \$1.5 million) and no change in the current federal law, at the husband's death the applicable credit amount would shelter \$1.5 million of assets passing to a credit shelter trust, while the balance of \$500,000 would pass to or for the benefit of the wife and qualify for the marital deduction, resulting in no federal estate tax in the husband's estate. At the wife's subsequent death (assume in 2005) her gross estate of \$1.1 million (assuming constant values) would be sheltered from federal estate tax by reason of her available applicable credit amount.

On the other hand, if the wife died first in 2005, her assets of \$600,000 would pass to a credit-shelter trust and would be sheltered from estate tax by the applicable credit amount, but the husband would continue to have a gross estate of \$2 million. If he died later in 2005, \$1.5 million would be sheltered from federal estate tax by the applicable credit amount, but the balance of \$500,000 would be subject to federal estate tax.

If the spouses in the above example were to reclassify their assets as marital property, the first decedent would have an estate subject to disposition of \$1.3 million. Assuming the death occurred in 2005, this entire amount would pass to the credit-shelter trust free of federal estate tax. In the survivor's estate (again assuming death in 2005), the survivor's \$1.3 million likewise would be sheltered from federal estate tax by the applicable credit amount. In larger estates, equalizing the spouses' respective estates can further facilitate estate tax planning by providing the opportunity to pay some estate tax in the first estate at lower marginal estate tax rates.

Of course, with scheduled increases in the federal applicable exclusion amount, and the uncertain future interplay of the Wisconsin estate tax, creating an example is a moving target. However, as a general principal, equalization of estates can be valuable for estate tax planning purposes. For a comprehensive discussion of the "decoupled" Wisconsin estate tax, see Michael W. Wilcox, *Wisconsin's New Estate Tax*, Wis. Law., Dec. 2001, at 10.

A similar analysis applies to a larger estate when the plan adopted contemplates the use of each spouse's GST exemption. By balancing the

sizes of the spouses' respective estates, optimal (or substantial) use of the GST exemption can be ensured regardless of which spouse dies first.

Using a marital property agreement to achieve balance in the size of the spouses' respective estates is an ideal planning technique since it does not require the retitling of assets held in either spouse's name alone. Each spouse can maintain management and control of his or her "own" assets during lifetime (subject to the duty of good faith and spousal remedies that apply to marital property assets). For cases involving assets held in the spouses' names together (for example, in a joint account), see section 10.31, *infra*.

## **5. Obtaining Full Adjustment in Basis of Marital Property Assets upon Death of One Spouse**

### **[§ 10.25]**

The IRS has recognized that, for federal tax purposes, Wisconsin marital property is community property. Rev. Rul. 87-13, 1987-1 C.B. 20. At the death of the first spouse, each marital property asset, not just the decedent's one-half interest, receives a basis adjustment (except for income in respect of a decedent, *see* I.R.C. § 1014(c)). This is favorable if the assets have increased in value above their tax basis but unfavorable if the assets have declined in value below their tax basis. The classification of assets as marital property can be done on an item-by-item basis, thereby avoiding the potential adverse consequences of the full adjustment for assets that have declined in value below the tax basis.

Assuming assets have increased in value, the full adjustment in basis allows the surviving spouse the opportunity to sell former marital property assets without realizing predeath capital gains. When the spouses' assets have been concentrated in a particular asset (e.g., stock of a particular company), the full basis adjustment provides greater opportunity for tax-free diversification by the survivor.

The full adjustment of basis can be particularly beneficial for depreciable property classified as marital property (e.g., investment real estate). The death of one spouse results in the establishment of a new tax basis, thereby allowing the decedent's estate and the surviving spouse to redepreciate the property for income tax purposes. *See supra* Ch. 9

## 6. Consideration of Creditor Rights [§ 10.26]

Reclassifying assets as marital property can expand the pool of assets available to satisfy certain obligations incurred by only one spouse. For example, family-purpose creditors can satisfy obligations from all marital property. Wis. Stat. § 766.55(2)(b). Tort creditors can satisfy claims from the tortfeasor's interest in marital property. Wis. Stat. § 766.55(2)(cm).

When liabilities (or potential liabilities) incurred by one spouse are a concern, the potential tax advantages of opting in to marital property classification for assets that otherwise would be the individual property or predetermination date property assets of the nonincurring spouse may be outweighed by such liability concerns. The better strategy for such spouses may be to preserve the individual property or predetermination date property status of assets of the spouse with less liability risk.

Further, for some spouses, concerns about potential liabilities may dictate the *manner* in which assets are reclassified as individual property. A creditor without advance knowledge of the provisions of a marital property agreement or unilateral statement (or who does not receive a copy thereof) cannot be adversely affected by the terms of the agreement or statement. Wis. Stat. § 766.55(4m). On the other hand, reclassification by certain other methods authorized by statute (for example, by gift, conveyance, or written consent) normally will be binding absent circumstances giving rise to remedies under fraudulent transfer laws. *See supra* ch. 6.

Hence, concerns about liabilities may affect both the decision whether to reclassify assets and the manner in which reclassification is accomplished.

## 7. Federal Preemption Issues [§ 10.27]

Certain assets are not readily subject to reclassification under the marital property law because the relative property rights of the spouses are defined by federal law rather than state law. *See* chapter 2, *supra*, for a general discussion of federal preemption as it relates to community property rights. *See* chapter 4, *supra*, for discussions of preemption issues related to certain government benefits. *See supra* chapter 2, and

*infra* § 10.110, for a discussion of federal preemption as it may apply to certain intellectual property rights.

In many instances, benefits under a qualified retirement plan governed by the Employee Retirement Income Security Act (ERISA), 29 U.S.C. §§ 1001–1461, may constitute a significant part of the spouses' estates. Because of the Supreme Court's decision in *Boggs v. Boggs*, 520 U.S. 833 (1997), planning for such assets in the context of a state community property law is problematic. For a discussion of planning for qualified plan assets, see §§ 10.132–10.147, *infra*.

### **C. Determining Appropriate Method of Classifying or Reclassifying Assets [§ 10.28]**

Assets may be classified or reclassified by a number of different methods. *See generally supra* ch. 2. The most common and straightforward means of classifying the assets of spouses is by use of a marital property agreement. The requirements for creating a binding marital property agreement are discussed in chapter 7, *supra*.

Although an enforceable marital property agreement will be binding as between the spouses, it will not be binding on creditors who do not have a copy of or advance knowledge of the provisions of the agreement. Wis. Stat. § 766.55(4m). Hence, in some instances, a different means of reclassifying assets may be desirable. *See infra* §§ 10.171–177.

Further, a marital property agreement requires the participation of both spouses. If one spouse is unwilling to participate, the other spouse may wish to use a unilateral statement under section 766.59 to effect the future classification of income from nonmarital property as his or her individual property. Like a marital property agreement, however, the unilateral statement is not binding on creditors without a copy of or advance knowledge of the terms of the unilateral statement. Wis. Stat. §§ 766.59(5), .56(2)(b).

## **D. Retitling Assets to Conform Title to Classification**

### **[§ 10.29]**

#### **1. In General [§ 10.30]**

When assets have been reclassified by marital property agreement or other means, it may be unnecessary to change the title of the asset. For example, if a husband's individual property asset is reclassified as marital property, he may continue to hold title to the asset, the effect of which is that he has management and control rights with respect to a marital property asset. In other instances, changing title to conform with classification may not be necessary but may nonetheless be advisable to facilitate later title transfers. For example, if spouses hold Wisconsin real estate as common law joint tenants and subsequently enter into a marital property agreement that classifies their assets (including the real estate) as marital property, the agreement controls the classification of the property. But on the death of one spouse, if the title has not been changed to conform with the classification, record title will still reflect a survivorship form of ownership. It may be necessary to record a court order establishing the classification of the real estate as marital property to satisfy title insurance requirements upon the subsequent disposition of the property. A more practical approach may be to have the spouses sign and record a deed confirming the classification of the property as marital property.

In other situations, changing the form of title may be necessary to avoid future ownership or tax disputes regarding the property rights of spouses and their successors in interest. For example, if an asset is held in the spouses' names together as joint tenants and then the spouses by marital property agreement reclassify the property as the individual property of one spouse, the property should be retitled in the name of that spouse alone.

#### **2. Joint Tenancies [§ 10.31]**

When assets are held in spouses' names together with the intent that those assets be owned as marital property without a right of survivorship, taking steps to have assets held in a manner that does not specify a right of survivorship may avoid future ownership or tax disputes.



When spouses have entered into a marital property agreement that classifies assets as marital property, the agreement, and not the title of the asset, determines the asset's classification. For example, when real estate is owned by spouses as joint tenants under section 700.17(2) and is later reclassified as marital property by a marital property agreement, the asset is marital property with no right of survivorship. Although retitling the real estate may facilitate future title transfers, retitling is not required. Similarly, if a stock certificate is owned by spouses as joint tenants under section 700.17(2), a marital property agreement reclassifying the spouses' assets as marital property changes the classification of the stock. The right of survivorship for joint tenancy assets specified by statute, *see* Wis. Stat. § 700.17(2), no longer applies because the classification of the asset has been changed.

Note, however, that if an asset is acquired after the spouses' determination date and the applicable document of title, instrument of transfer, or bill of sale expresses an intent to establish a joint tenancy exclusively between the spouses, absent a contrary provision in a marital property agreement, the asset is survivorship marital property. Wis. Stat. § 766.60(4)(b)1.a. For example, if spouses enter into a general opt-in marital property agreement before or after acquiring a security owned as survivorship marital property pursuant to section 766.60(4)(b)1.a. and the agreement is silent regarding any right of survivorship, the form of holding title will control the right of survivorship. Unlike the effect on a predetermination date security owned by spouses as joint tenants under section 700.17(2)—in which case an opt-in marital property agreement serves to change the classification of the security from joint tenancy to marital property—a general opt-in marital property agreement does not change the classification of the security already owned by the spouses as survivorship marital property. Survivorship marital property is not a separate classification but merely marital property with a right of survivorship. Hence, absent a provision in the marital property agreement providing otherwise, *see* Wis. Stat. § 766.60(4)(b)1., the spouses' agreement that such assets are classified as marital property does not alter the right of survivorship.

### **3. Brokerage Accounts [§ 10.32]**

Other assets may present a more difficult case because the right of survivorship may arise from a contractual arrangement as opposed to a statutory classification. For example, the terms of a brokerage account

agreement may specify a right of survivorship. Does entering into a marital property agreement classifying assets generally as marital property override the contractual right of survivorship in the brokerage agreement so that the will of the first deceased spouse disposes of one-half of the assets in the brokerage account? Or, does the marital property agreement simply cause the assets of the account to be classified as marital property but with the deceased spouse's interest passing at death in accordance with the brokerage agreement to the surviving spouse?

Although its context is a tax dispute, the U.S. Tax Court's decision in *Estate of Richman v. Commissioner*, 66 T.C.M. (CCH) 527 (1994), illustrates the uncertainty that may be created when the dispositive provisions in a brokerage-account agreement differ from the dispositive provisions under the deceased spouse's will in a community property state. In *Richman*, Texas community property had been invested in a Massachusetts business trust. The governing instrument creating the business trust provided that the trust and the rights of all parties would be determined under the laws of Massachusetts (which is not a community property state). The tax controversy arose because the deceased husband's will left his share of community property in a manner that did not qualify for the marital deduction. The decedent's estate maintained that the decedent's interest in the trust passed pursuant to the terms of the investment application, which specified that the applicants would be joint tenants with right of survivorship. The tax court concluded that the choice of law provision in the application controlled. As a result, the interest passed to the surviving wife and qualified for the marital deduction.

In a decision not involving an analysis under chapter 766, the Wisconsin Court of Appeals concluded in *Templeton v. Moccero (In re Estate of Moccero)*, 168 Wis. 2d 313, 321, 483 N.W.2d 310 (Ct. App. 1992), that a joint account held by spouses at a brokerage firm passed by survivorship to the husband at the wife's death. This was so even though the circuit court found that the husband, who contributed all the property to the account, had intended to make a gift of one-half of the property to his wife. The wife's daughter argued that one-half of the account was required to be inventoried as part of her mother's estate and thus was subject to disposition by her mother's will. The circuit court concluded that the account was a joint account with right of survivorship. The court of appeals, quoting section 705.04(1) (which by its terms applies only to joint accounts at financial institutions), held that the circuit court's finding was not clearly erroneous and that the circuit court had correctly

applied the law. Despite the court's reference to section 705.04, it is clear that the court of appeals concluded that the account was a joint tenancy. *See also First Wis. Trust Co. v. United States*, 553 F. Supp. 26 (E.D. Wis. 1982) (holding that, in gift tax dispute, solely owned stock transferred to brokerage account in spouses' names denominated as "joint tenancy with right of survivorship" resulted in spouses becoming joint tenants with respect to stock).

From a planning standpoint, questions about the effects of dispositive terms in a brokerage-account agreement can be avoided by either inserting specific provisions into the marital property agreement or by retitling an asset or account to conform the title with the intent regarding survivorship. One possibility is to specify in the marital property agreement the incidents of survivorship for assets held in certain forms. For example, the agreement might provide:

Property held by the Parties jointly with the right of survivorship (for example, but not necessarily limited to, joint tenancy property, joint bank accounts, joint brokerage accounts which provide for a right of survivorship, and survivorship marital property), whether such joint ownership was established before or after the Parties' determination date, shall be survivorship marital property.

If the goal is to avoid any right of survivorship for marital property assets, the spouses might attempt to override the right with provisions in a marital property agreement. The problem with this method, however, is that the third party may insist on a court determination of ownership rights before acknowledging the right of the personal representative of the first deceased spouse to manage and control the deceased spouse's interest in the former marital property asset. Further, as discussed below, in the case of joint accounts at financial institutions governed by chapter 705, the statutes create questions as to the effectiveness of such a provision in a marital property agreement when it comes to overriding the presumptive right of survivorship. If this method is used and the intent is to have the decedent's interest in a jointly held asset pass other than to the surviving spouse, having the survivor execute a disclaimer following the death of the first spouse will eliminate uncertainty regarding the disposition of the decedent's interest in the asset.

The more certain approach to eliminating rights of survivorship is to simply have spouses hold title to marital property assets in a form that does not include a right of survivorship. A marital property asset may be

held in the name of one spouse alone (and, if the spouses desire joint management, the holding spouse can grant the nonholding spouse a durable power of attorney). Or, if the spouses desire to have both names on the title and to jointly manage an asset, it may be held in a joint form that does not include a right of survivorship. Wisconsin real estate may be held in the form “Husband and Wife, as marital property.” Wis. Stat. § 766.60(2). Publicly traded securities and brokerage accounts normally will not have “marital property” as an optional form of holding title to property, but spouses may nonetheless hold title to marital property assets as tenants in common. Wis. Stat. § 766.60(4)(b)1.b. If spouses have created a joint revocable trust as part of their estate plan, marital property assets may be held by the spouses as trustees of the trust. *See generally infra* §§ 10.55–10.63. At the death of one spouse, the terms of the trust will specify the disposition of the deceased spouse’s one-half of former marital property assets.

#### **4. Accounts in Financial Institutions [§ 10.33]**

Chapter 705 governs multiple party “accounts” in “financial institutions” (both being defined terms in section 705.01). It appears that the accounts described in chapter 705 do not include brokerage accounts since brokerage firms do not appear to be included within the definition of *financial institution* under section 705.01(3). Moreover, section 766.01(9)(b) does not appear to regard *accounts* under section 705.01 as including brokerage accounts. But see *Estate of Moccero*, 168 Wis. 2d at 321, discussed at section 10.32, *supra*, in which the court looked to chapter 705 in resolving a dispute regarding entitlement to assets in a brokerage account; see also *Reichel v. Jung (In re Estate of Jung)*, 2000 WI App 151, 237 Wis. 2d 853, 616 N.W.2d 118, discussed *infra*, in which the court of appeals included an insurance company within the term financial institution.

In Wisconsin financial institutions (including banks and credit unions) whose accounts are governed by chapter 705, spouses may open a “marital account” as an alternative to a joint account. *See generally supra* ch. 2. At the death of one spouse, the deceased spouse’s one-half interest in the account is subject to administration, and the surviving spouse continues to own his or her one-half interest. Wis. Stat. § 705.04(2m).

Section 705.04(1) provides in part that “[s]ums remaining on deposit at the death of a party to a joint account belong to the surviving party or parties as against the estate of the decedent unless there is clear and convincing evidence of a different intention at the time the account is created.” What is the effect of a marital property agreement classifying assets generally as marital property without right of survivorship when the agreement is entered into *after* a joint account between spouses has been established? Under the statute, the right of survivorship should continue to apply because assets of the account belong to the surviving owner absent “clear and convincing evidence of a different intention *at the time the account is created*.” (Emphasis added.) Uncertainty can be avoided by causing title to be held in a manner consistent with the spouses’ expectations concerning the right of survivorship.

Uncertainty regarding classification can further be avoided by keeping one spouse’s nonmarital property assets (for example, inherited funds) from a joint bank account held by the spouses together. Although placement of funds in a joint bank account is not a statutory method for reclassifying assets, case law has suggested that reclassification may be effected in this manner. See *Lloyd v. Lloyd (In re Estate of Lloyd)*, 170 Wis. 2d 240, 487 N.W.2d 647 (Ct. App. 1992), *supra* § 3.14.

In *Estate of Jung*, 2000 WI App 151, 237 Wis. 2d 853, the Wisconsin Court of Appeals considered an appeal by the deceased husband’s children from the circuit court’s ruling that the decedent’s surviving wife, and not the children, were entitled to receive the proceeds of an annuity of which the decedent was the owner. The husband and wife had entered into a “Marital Property Classification Agreement” in which they effectively adopted an individual property regime based on title, and the husband’s will left the residue of his estate to his children. However, under the annuity contract, the husband was the first annuitant and the wife was the co-annuitant, and the terms of the annuity contract provided for a right of survivorship in favor of the co-annuitant. Affirming the circuit court, the court of appeals concluded that the annuity contract’s survivorship provision constituted a “nonprobate transfer” under section 705.20 (now section 705.10) (even though “annuities” are not specifically mentioned in that section among the types of property that can be transferred by nonprobate means). The court further concluded that, under section 705.04, the annuity contract constituted a joint account that passed to the survivor by operation of law, concluding that the insurance company that issued the annuity was a financial institution within the meaning of section 705.01.

2005 Wisconsin Act 216, section 35, added a new subsection (4) to section 705.10 (formerly section 705.20), expanding the manner in which a nonprobate transfer can be confirmed following death.

## **V. Transfers by Will [§ 10.34]**

### **A. Property Subject to Disposition by Will [§ 10.35]**

#### **1. Decedent's One-half Interest in Marital Property Assets [§ 10.36]**

Each spouse owns a present undivided one-half interest in each marital property asset. Wis. Stat. § 766.31(3). Section 766.31(3)(b) allows for the postdeath allocation of marital property assets on an aggregate basis, rather than on an item-by-item basis. As a result, a spouse generally has a power of testamentary disposition over one-half of each marital property asset, with the other one-half continuing to belong to the survivor. But there are exceptions. If the marital property asset is an interest in a deferred-employment-benefit plan or an individual retirement account (IRA) traceable to the rollover of a deferred-employment-benefit plan, the interest of the nonemployee spouse terminates at death unless a marital property agreement provides otherwise. Wis. Stat. §§ 766.31(3), .62(5). If the marital property asset is an interest in a life insurance policy and the noninsured spouse dies first, the deceased spouse's interest in the policy is limited by statute to a share of the cash value unless a marital property agreement provides otherwise. Wis. Stat. § 766.61(7). If the marital property asset is a personal injury recovery for loss of income, the uninjured spouse's interest in the recovery terminates at death. Wis. Stat. § 766.31(7m). If a marital property asset is held as "survivorship marital property," at the death of the first spouse, the decedent's one-half interest passes by operation of law to the survivor. Wis. Stat. § 766.60(5). Likewise, the use of other nonprobate means of transferring property at death may affect a spouse's power of testamentary disposition over his or her share of a marital property asset, such as the use of a will-substitute agreement under section 766.58(3)(f) or a funded revocable trust.

If the surviving spouse has asserted the right to the deferred marital property elective share under section 861.02, the value of the deceased spouse's interest in marital property passing to the surviving spouse from

decedent's estate is applied toward initial satisfaction of the elective share. Wis. Stat. § 861.06(2).

An important consideration for spouses who view their assets as being owned on the basis of title is that the first deceased spouse's will disposes of his or her interest in all marital property assets subject to administration, whether titled in the name of the deceased spouse or in the name of the survivor. If the residuary clause of the first deceased spouse does not pass the residue to the survivor, the survivor may be surprised by the result. If the spouses are working together on their estate plan, the surprise can be avoided if the estate planner educates the spouses as to how the law works. Once they understand the potential impact of the law, they may wish to address certain property rights at death with specific provisions in their wills, in a will-substitute agreement, or in a marital property agreement.

## **2. Decedent's Individual Property Assets and Predetermination Date Property Assets Not Subject to Elective Rights [§ 10.37]**

A spouse is free to transfer his or her individual property assets, by will, without interference by the surviving spouse. The same is true with respect to predetermination date property assets that would have been classified as individual property had they been acquired when chapter 766 applied (*deferred individual property*, Wis. Stat. § 861.018(2)). In either case, such individual property and deferred individual property assets are not part of the augmented deferred marital property estate, Wis. Stat. § 861.02(2), and they are not available to satisfy the deferred marital property elective share if the surviving spouse makes the election under section 861.02. *See* Wis. Stat. § 861.06. However, to the extent that such assets pass to the surviving spouse, their value is included in determining whether the elective share has been satisfied (along with any such assets passing to the surviving spouse by nonprobate means as well). Wis. Stat. § 861.06.

### **3. Decedent's Predetermination Date Property Assets Subject to Elective Rights [§ 10.38]**

As revised by 1997 Wisconsin Act 188, the deferred marital property election under chapter 861 allows a surviving spouse to take an *amount* equal to not more than one-half the augmented deferred marital property estate. *See* Wis. Stat. § 861.02(1). (This is in contrast to the former deferred marital property election, which allowed the surviving spouse to elect up to a one-half interest in each item of deferred marital property that was subject to administration.) However, assets disposed of by a deceased spouse's will that constitute part of the augmented deferred marital property estate are available to satisfy the deferred marital property elective share. Wis. Stat. § 861.06. Thus, the deceased spouse's will disposes of each item of deferred marital property in accordance with the terms of the will, subject to the possibility that the asset may be required to satisfy the deferred marital property elective share.

## **B. Specific Bequests and Devises [§ 10.39]**

### **1. To Spouse [§ 10.40]**

If the deceased spouse's will gives a specific asset to the surviving spouse, the classification of the property given has little significance from the standpoint of the ultimate ownership of the asset. If the asset is the decedent's individual property, the entire asset is subject to administration in the decedent's estate and passes pursuant to the terms of the will to the spouse. If the asset is predetermination date property, the entire asset is likewise subject to administration in the decedent's estate and passes pursuant to the terms of the will to the spouse, whether or not it is part of the augmented deferred marital property estate. If the asset is marital property of the decedent and surviving spouse, one-half of the asset is subject to administration in the decedent's estate and passes pursuant to the terms of the will to the spouse. The surviving spouse already owns the other one-half interest in the asset.

If the surviving spouse has asserted the elective right to the deferred marital property elective share under section 861.02, the value of the deceased spouse's interest in a marital property asset specifically



bequeathed to the surviving spouse from the decedent's estate is applied toward initial satisfaction of the elective share. Wis. Stat. § 861.06(2)(b).

From an estate tax perspective, if the asset is nonmarital property, the entire value of the asset is includible in the decedent's gross estate. If the asset is marital property, only one-half the value is includible in the decedent's gross estate. *See supra* ch. 9. In either case, the value passing to the surviving spouse qualifies for the marital deduction under I.R.C. § 2056 so that there is no estate tax associated with the transfer. See, however, section 10.131, *infra*, regarding limitations on the availability of the marital deduction in the case of assets passing to a spouse who is not a U.S. citizen.

From the standpoint of the income tax basis of the asset, the result is the same whether the asset is marital or nonmarital property—that is, the entire asset receives a basis adjustment by reason of the decedent's death. *See generally supra* ch. 9.

Spouses' marital property assets may include items titled in one spouse's name alone that the other spouse clearly would want the titled spouse to own outright in the event of the death of the nontitled spouse. For example, a husband holds a membership interest in a golf club that was acquired with marital property assets and that is devisable (often such interests are not devisable). The residuary clause of the wife's will pours assets to a revocable trust, which in turn allocates assets between a qualified terminable interest property (QTIP) marital trust and a credit-shelter trust. Absent a specific provision in the wife's will (or in the revocable trust) to the contrary, if the wife predeceases the husband, the wife's interest in the golf club membership would pass to the revocable trust and would be allocable either to the QTIP trust or to the credit-shelter trust, which is not likely to be the intended result. The husband may be forced to purchase the interest from the wife's estate in order to own it outright. The spouses could have prevented this result by including a specific provision in the wife's will, such as, "I give and bequeath to my husband, John, if he survives me, any interest I may own in ABC Golf Club." Note, however, that if the wife has insufficient assets to fully fund the credit-shelter trust, forcing the husband to buy the wife's marital property interest from her estate or from the credit-shelter trust may provide an additional opportunity to shelter assets from estate tax in the husband's estate.

## **2. To Third Party [§ 10.41]**

If an asset is bequeathed to a third party, its classification is important, because it may determine whether the testator's intent is carried out. If the asset is the decedent's individual property or is predetermination date property that is not part of the augmented deferred marital property estate (i.e., "deferred individual property" under section 861.018(2)), the asset passes under the decedent's will to the specified beneficiary and is not available to satisfy the deferred marital property elective share under section 861.02(1). Wis. Stat. § 861.06(2). If the asset is predetermination date property that is part of the augmented deferred marital property estate, the asset passes under the decedent's will to the specified beneficiary, subject, however, to the possibility that it may be applied toward satisfaction of the deferred marital property elective share if the elective right under section 861.02(1) is asserted by the surviving spouse. Wis. Stat. § 861.06(3).

If the asset is a marital property asset, the bequest or devise of it to a third party will transfer only the decedent's one-half interest in the asset to the third party. The specified beneficiary becomes a co-owner with the surviving spouse, which in many cases will not be the decedent's intent. This result can be avoided by having the spouses reclassify the asset as the individual property of the party who intends to make a gift of the asset in his or her will.

## **C. Pecuniary Bequests [§ 10.42]**

### **1. To Spouse [§ 10.43]**

A pecuniary bequest to the surviving spouse will be satisfied from the decedent's interest in marital property assets or the decedent's nonmarital property assets. If the surviving spouse has asserted the elective right to the deferred marital property elective share under section 861.02, amounts passing to the spouse from the decedent's estate are applied toward initial satisfaction of the elective share. Wis. Stat. § 861.06(2).

## **2. To Third Party [§ 10.44]**

A pecuniary bequest to a third party will be satisfied from the decedent's interest in marital property assets or the decedent's nonmarital property assets. These may include assets titled in the surviving spouse's name alone that were regarded by the spouses as belonging to the titled spouse. Hence, the potential exists for unanticipated consequences for the survivor when he or she learns that one-half of his or her solely titled asset is available to satisfy the pecuniary bequest. This result can be avoided by having the spouses reclassify the asset as the individual property of the spouse who holds title to the asset.

### **D. Formula Bequests [§ 10.45]**

#### **1. To Spouse [§ 10.46]**

A formula bequest to the surviving spouse (for example, a bequest designed to make optimal use of the marital deduction and applicable credit amount) will be satisfied from the decedent's interest in marital property assets or the decedent's nonmarital property assets. If the surviving spouse has asserted the elective right to the deferred marital property elective share under section 861.02, amounts passing to the spouse from the decedent's estate are applied toward initial satisfaction of the elective share. Wis. Stat. § 861.06(2).

#### **2. To Third Party [§ 10.47]**

A formula bequest to a third party will be satisfied from the decedent's interest in marital property assets or the decedent's nonmarital property assets. These may include assets titled in the surviving spouse's name alone that were regarded by the spouses as belonging to the titled spouse. Hence, as with a pecuniary bequest, the potential exists for unanticipated consequences for the survivor when he or she learns that one-half of his or her solely titled asset is available to satisfy the formula bequest. This result can be avoided by having the spouses reclassify the asset as the individual property of the spouse who holds title to the asset.

## **E. Residuary Bequests [§ 10.48]**

### **1. To Spouse [§ 10.49]**

A residuary bequest to the surviving spouse passes, to the surviving spouse, the decedent's interest in marital property assets and nonmarital property assets that are not the subject of specific, pecuniary, or formula bequests. If the surviving spouse has asserted the elective right to the deferred marital property elective share under section 861.02, amounts passing to the spouse from decedent's estate are applied toward initial satisfaction of the elective share. Wis. Stat. § 861.06(2).

### **2. To Third Party [§ 10.50]**

A residuary bequest to a third party passes, to the third party, the decedent's interest in marital property assets and nonmarital property assets that are not the subject of specific, pecuniary, or formula bequests. These assets may include assets titled in the surviving spouse's name alone that were regarded by the spouses as belonging to the titled spouse. This can result in an unpleasant surprise to the survivor when he or she learns that one-half of his or her solely titled asset is available to satisfy the residuary bequest. Likewise, there may be marital property assets, titled in the deceased spouse's name alone, that were regarded by the spouses as belonging to the titled spouse. The residuary beneficiary will be entitled to receive only one-half of those assets, which may not be the intended result.

To avoid such unanticipated results, the spouses can reclassify assets to make the classification coincide with their view of ownership and their expectations of how the property should pass at death.

## **F. Spouse as Personal Representative [§ 10.51]**

One responsibility of the personal representative of a decedent's estate is to file with the court an inventory of the decedent's property, including the property's value as of the date of death and indicating which assets are marital property. Wis. Stat. § 858.01. Absent a comprehensive marital property agreement classifying the assets, determining the assets' classification upon death may be a daunting task.

If the surviving spouse is not the sole beneficiary of the decedent's estate, there is a potential conflict in naming the spouse as the personal representative since he or she must determine which of the assets held either by the decedent or the survivor are classified as marital property. In many situations—particularly those in which the spouses worked together in their estate planning—this potential conflict poses little concern. In other situations, however—for example, second marriages in which there are children from the first marriage—naming the spouse as sole personal representative could prove troublesome. In those situations, the testator might designate someone else or at least require the appointment of a co-personal representative to serve with the surviving spouse.

### **G. Equitable Election [§ 10.52]**

Wisconsin's equitable election statute, section 853.15, is discussed in detail in chapter 12, *infra*. The statute applies when a will “clearly purports” to transfer property that actually belongs to another person who is also a beneficiary under the will. If the statute applies, the other person is forced to elect between (1) keeping his or her interest in the specifically devised property and forfeiting his or her beneficial interest under the will, or (2) forfeiting his or her interest in the specifically devised property and accepting his or her beneficial interest under the will.

If a testator wishes for the equitable election statute to apply, his or her intention should be clearly stated in the will. Inadvertent application of the statute should be avoided in will drafting. Wisconsin's marital property system creates the potential for the inadvertent application of the equitable election statute in the case of a specific bequest or devise of property that the testator spouse believes to be his or her own but that in fact belongs to the spouses as marital property. A convenient way to clearly override the statute is to include a provision in each spouse's will stating, “It is not my intention to dispose of my spouse's interest in any marital property assets.”

## **VI. Revocable Living Trusts [§ 10.53]**

### **A. In General [§ 10.54]**

Revocable living trusts are frequently used in estate planning. For an excellent discussion of the advantages and disadvantages of revocable living trusts, see Price, *supra* § 10.1, at sections 10.7–.17. The discussion here focuses on the marital property issues related to the use of revocable living trusts. The basic points to be elaborated upon in the following discussion are the following:

1. Marital property assets and income in a revocable living trust remain marital property while in the trust. *See* Wis. Stat. § 766.31(5).
2. Marital property assets in a properly prepared revocable living trust are eligible for the full adjustment in basis afforded marital property assets in the Internal Revenue Code. The provisions of one joint revocable trust holding community property that were determined to preserve qualification for the full basis adjustment are described in Rev. Rul. 66-283, 1966-2 C.B. 297.
3. If the revocable living trust contains marital property assets, the trust instrument should deal with the disposition of property upon the death of each spouse. A joint trust created by the spouses generally is the best way to do that. *See* sample form at section 10.180, *infra*.

### **B. Effect of Transfer of Marital Property Assets to Revocable Trust [§ 10.55]**

The transfer of property to a trust does not by itself change the classification of the property. Wis. Stat. § 766.31(5). Assuming there is nothing in the trust instrument that would change the classification, assets transferred to a revocable living trust retain their classification while held by the trustee. The Comment to section 4 of the Uniform Marital Property Act (UMPA reprinted in appendix A, *infra*) also addresses this issue.

This conclusion is not inconsistent with section 766.70(6)(a), which provides a remedy for gifts of marital property assets to third persons. Because the donor retains the power to withdraw, there is no gift when a

marital property asset is transferred to a revocable trust. A transfer to a revocable living trust is an exercise of the spouse's power to manage and control. *See generally supra* ch. 4.

For a discussion of grantor trust issues raised by the transfer of marital property assets to a trust, see chapter 9, *supra*.

### **C. Management and Control of Assets Held in Revocable Trust [§ 10.56]**

The trustee of a trust has the authority to manage and control marital property assets transferred to the trust. Wis. Stat. § 766.51(3). Generally, the classification of the property in the possession or control of the trustee does not affect the trustee's right and duty to administer, manage, and distribute the property in accordance with the terms of the governing instrument, Wis. Stat. § 766.575(2), although this may be altered by the terms of the governing instrument, by a court order, or pursuant to the claim procedure set forth in section 766.575(3).

### **D. Joint Revocable Living Trust vs. Separate Revocable Living Trusts [§ 10.57]**

#### **1. Joint Trust [§ 10.58]**

If spouses own assets as marital property and wish to transfer them to a revocable living trust (as a means of managing assets or for the purpose of avoiding probate, or both) a joint trust (created by the spouses as joint grantors) is superior to separate trusts (one created by each spouse). By using a joint trust, the spouses can easily address in the trust instrument what will happen to each spouse's interest in former marital property assets upon the death of the first spouse, as well as on the death of the survivor. Assuming there is nothing in the trust instrument that would change the assets' classification, assets held by the trust receive the full adjustment in basis on the death of the first spouse to die. *See* Rev. Rul. 66-283, 1966-2 C.B. 297. For a sample joint revocable living trust form, see section 10.180, *infra*.

## 2. Separate Trusts [§ 10.59]

Usually a joint trust created by the spouses together as grantors is the best approach when spouses wish to transfer marital property assets to a revocable living trust. However, there may be circumstances in which the use of a separate revocable living trust created by one spouse alone is warranted. For example, an estate plan adopted before the spouses were subject to the marital property law may involve separate revocable living trusts, and the spouses may prefer simply to amend their existing documents rather than to start over. Or one spouse may have significant individual property assets (for example, a large inheritance) that he or she wants to manage and control separately in his or her own trust along with other assets that may be marital property. A third possibility is that the spouses may not be of the same mind about dispositive provisions and therefore wish to have their own separate trusts. Whatever the circumstances, if it is possible that a spouse's solely created revocable living trust will hold marital property assets, the trust instrument should address the disposition of each spouse's one-half interest in those assets regardless of which spouse dies first.

If one spouse has significant individual property assets (for example, an inheritance) that he or she wants to preserve as individual property, placing them in a separate revocable living trust is a convenient way of segregating and tracing the assets. In creating such a trust, however, it is important to keep in mind the general rule that income from nonmarital property is marital property. *See* Wis. Stat. § 766.31(4). Unless steps have been taken to reclassify the income from nonmarital property as individual property, the provisions of the trust agreement should require that the net income of the trust be distributed to the grantor, so that it can be placed in an account holding only marital property funds.

To reclassify the income from individual property assets held by the trust, the grantor could execute a unilateral statement under section 766.59 to reclassify the income as individual property, or the spouses could enter into a marital property agreement that classifies the income as individual property. *See* chapter 2, *supra*, for a discussion of classification by unilateral statement and of classification by marital property agreement. Even if income is classified as individual property it may nonetheless be prudent to require the trustee to separately account for and trace the investment and reinvestment of income, since a unilateral statement would have no effect on property division in the



event of dissolution, and a marital property agreement could ultimately be declared unenforceable.

## **E. Death of Spouse When Marital Property Assets Are Held in Single-grantor Revocable Trust [§ 10.60]**

### **1. Death of Grantor Spouse [§ 10.61]**

If the sole grantor of a revocable living trust dies before his or her nongrantor spouse, the trust becomes irrevocable by reason of the grantor's death. The surviving spouse owns a one-half interest in any former marital property assets as a tenant in common with the trustee. Wis. Stat. § 861.01. In addition to providing for the disposition of the grantor spouse's interest in property held by the trust, the trust instrument should provide for the disposition of the surviving spouse's marital property interest either to the spouse directly or to a trust that the surviving spouse controls.

For a discussion of issues relating to the administration of a former revocable living trust holding former marital property assets upon the death of the grantor, see generally chapter 12, *infra*. For a discussion of the remedy available to the surviving spouse when a revocable living trust established by his or her spouse fails to acknowledge the survivor's marital property interest, see section 8.48, *supra*.

### **2. Death of Nongrantor Spouse [§ 10.62]**

If the nongrantor spouse dies before the grantor of a revocable living trust holding marital property assets, the trust remains revocable and the surviving spouse's one-half interest in former marital property is not subject to administration. Wis. Stat. § 861.01(1). However, the personal representative of the deceased nongrantor spouse succeeds to the interest of the decedent in all property of the decedent. Wis. Stat. § 857.01. This would include the decedent's one-half interest in all former marital property held in the surviving grantor spouse's revocable living trust. From a drafting standpoint, the deceased spouse's property interest can be addressed by including a provision in the grantor spouse's trust instrument directing the disposition of the decedent's interest in former marital property. The trust instrument should provide for the transfer of

the decedent's interest in former marital property either to the decedent's personal representative or to a revocable living trust that was created by the decedent.

### **3. Flexibility to Distribute Assets Based on Aggregate Value Rather Than Item by Item** **[§ 10.63]**

As noted in section 10.10, *supra*, 2005 Wisconsin Act 216, section 42, amended section 766.31(3) to permit distribution on an aggregate rather than on an item-by-item basis so as to allow more flexibility in the administration of the estate of the first deceased spouse. In drafting a trust agreement designed to hold marital property assets, the drafter may wish to include among the powers of the trustee something such as the following:

To make any division, allocation, or distribution of property in cash, in kind, or both, and to allocate all or any part of any item or kind of property to any trust, trust share, or beneficiary, without regard to the basis of the property for income tax purposes, and to make non-pro rata distributions and determine the fair market values of any such property incident to any such division, allocation, or distribution (*including, without limitation, with respect to marital property assets upon the death of the first deceased spouse, some or all of which may be divided on the basis of aggregate value rather than divided item by item, in a manner consistent with Wisconsin law*).

## **VII. Will Substitute Agreements [§ 10.64]**

### **A. In General [§ 10.65]**

Spouses may provide in a marital property agreement for a nontestamentary disposition of property upon the death of either of them, including the nontestamentary disposition of after-acquired property. Wis. Stat. § 766.58(3)(f). If they include such a provision in the agreement, the marital property agreement acts as the dispositive instrument of transfer with respect to assets covered by the provision, like a will. The spouses may also provide for a nontestamentary disposition of property upon the death of the second spouse to die. However, section 766.58(3)(f) permits the second spouse to unilaterally

amend the marital property agreement after the death of the first spouse unless the marital property agreement prohibits such amendment and except to the extent property is held in a trust established by the marital property agreement. For a detailed discussion of will substitute agreements, see generally chapter 7, *supra*. Such agreements are known colloquially in Wisconsin as “Washington wills” because Washington state law provides for a similar type of spousal agreement.

Section 766.58(3)(f) may be applied to all types of property, including marital property, individual property, and predetermination date property. A marital property agreement can classify property and provide for its disposition, property can be transferred by agreement to any person or to a trust, and the terms of the trust may be contained in the agreement or may be independent of the agreement. A marital property agreement may be amended or revoked only by a later marital property agreement. Wis. Stat. § 766.58(4).

## **B. Tax Consequences [§ 10.66]**

The tax consequences of making a nontestamentary disposition by marital property agreement must be considered carefully. Is a provision regarding a nontestamentary disposition merely contractual? Or is the document presently dispositive (in the same sense that a deed conveying an interest in real estate is dispositive)? The distinction is significant. In *Pyle v. United States*, 766 F.2d 1141 (7th Cir. 1985), the U.S. Court of Appeals for the Seventh Circuit held that federal gift tax was payable by the surviving spouse upon the death of the first spouse to die because the spouses had a joint will and a contract not to revoke the will. The court held that, under Illinois law, the joint will combined with the contract not to revoke created a legal life estate in the surviving spouse and remainder interest in the persons who took the property after the death of the surviving spouse. The gift tax was assessed on the remainder interests. The court held that the provisions of the joint will were dispositive, not merely contractual.

Section 766.58(3)(f) addresses the *Pyle* issue by providing that the surviving spouse may amend the marital property agreement with respect to property to be disposed of at the death of the surviving spouse unless the marital property agreement expressly provides otherwise and except to the extent property is held in a trust established under the agreement. This right to amend, unless eliminated by the agreement, should prevent

any gifts intended to take effect at the survivor's death from being treated as complete for tax purposes at the death of the first spouse to die. If the survivor's right to amend is eliminated, adverse tax consequences may result.

### **C. Adding Flexibility to Will Substitute Provisions [§ 10.67]**

If a will substitute provision is to be included in a marital property agreement, consideration should be given to whether each spouse can take unilateral action so as not to be bound by the provision. For example, the agreement can specify that the will substitute provision applies only so long as a will exists that provides for a similar disposition. The agreement can provide that, if the will is changed, the will substitute provision no longer applies. (As discussed in section 10.69, *infra*, a backup will is recommended). Or, each spouse can have a right to revoke or modify the will substitute provision as to his or her own assets upon notice to the other spouse.

If the will substitute provision does not provide unilateral ways for a spouse to eliminate the provision, each spouse will be bound unless the other spouse consents to a change. Each spouse will have the ability to veto the other spouse's desire to change the will substitute provision. By contrast, a will can be changed at any time by a person without the knowledge or consent of his or her spouse.

### **D. Limiting Scope of Will Substitute Provision [§ 10.68]**

The application of a will substitute agreement should be limited to assets that would otherwise be subject to administration. On its face, section 766.58(3)(f) seems to permit the spouses to enter into a marital property agreement disposing of assets not subject to administration. In most cases, the spouses would not want the agreement to apply to nonprobate dispositions arranged either before or after the agreement is executed. Examples of such nonprobate dispositions include retirement plan beneficiary designations, life insurance beneficiary designations, and survivorship marital property.

### **E. Additional Considerations Regarding Use of Will Substitute Agreement [§ 10.69]**

Some things to consider when contemplating the use of, or preparing, a marital property agreement as a will substitute agreement include the following:

1. The agreement should state that the spouses intend to make a nontestamentary disposition pursuant to section 766.58(3)(f).
2. An advantage of a will substitute agreement over a will exists if one spouse subsequently becomes incompetent. In that event, the spouse's will substitute agreement can be amended despite the incompetency if the amendment is by a guardian with the approval of the court. *See* Wis. Stat. ch. 54. It is not possible for a guardian to amend or revoke a ward's will. *Id.*
3. Assets transferred by will substitute agreement pass by operation of law and are not subject to probate administration. The statutes provide for summary proceedings to confirm the transfer of assets by the agreement. Certain types of property may be transferred administratively (using a Form HT-110), including "an interest in any real property, a vendor's interest in a land contract, an interest in a savings or checking account, an interest in a security or a mortgagee's interest in a mortgage, including an interest in survivorship marital property." Wis. Stat. § 867.046(2). Other types of property require a summary confirmation proceeding before the court as contemplated by section 867.046(1m). *See Maciolek v. City of Milwaukee Employees' Ret. Sys. Annuity & Pension Bd.*, 2005 WI App 74, 280 Wis. 2d 585, 695 N.W.2d 875, *aff'd*, 2006 WI 10, 288 Wis. 2d 62, 709 N.W.2d 360. Subsequent to the Wisconsin Supreme Court's decision in *Maciolek*, the legislature modified the statute to expand permissible uses of a Form HT-110. *See infra* § 12.174.
4. A backup will to the agreement is advisable. A will can provide for some things a will substitute agreement cannot, such as the appointment of a personal representative or guardian. If the coverage of the will substitute agreement is limited, an all-inclusive backup, used in conjunction with the will substitute agreement, is necessary to avoid a partial intestacy. As discussed above, the

agreement and the will can be coordinated to eliminate a possible inconsistency between the will and the agreement.

5. A special administration pursuant to section 867.07 can be helpful in conjunction with a will substitute agreement. Often, it is necessary that someone with plenary authority represent the decedent regarding matters not involving the administration of assets. A representative may be needed to enter and inventory the decedent's safe deposit box, pick up mail at the post office, leave a forwarding address at the post office, execute a mortgage satisfaction, etc. If the will substitute agreement transfers the decedent's assets, the special administrator's duties will be strictly ministerial and he or she cannot be liable to the beneficiaries for asset management. If the will substitute agreement does not transfer all the decedent's assets, and some assets are subject to administration, a special administrator is usually not appropriate. A personal representative should be appointed.
6. A "pour-over" will substitute agreement can be useful when used in conjunction with an unfunded or partially funded revocable living trust when the trust contains dispositive provisions intended to avoid probate administration at death. The will substitute agreement can be used in lieu of funding the trust or to transfer assets that were inadvertently left out of the trust. If the trust is funded, assets such as tangible personal property can be left out of the trust and transferred later by the will substitute agreement.
7. One advantage of probate administration is the certainty and finality achieved by having a recognized procedure for the judicial determination of the classification of the decedent's and surviving spouse's assets and the adjudication of creditors' claims. In a situation in which the classification of assets under the marital property law may be disputed, for example, a second marriage with each spouse having children by a previous marriage, a probate administration may be the preferred way to transfer assets at death.
8. A Wisconsin will substitute agreement may not be recognized in another state in which the decedent owns real estate or to which the spouses later move, even if its terms specify that the agreement's effectiveness continues notwithstanding a change in domicile. This is another reason why it is important to have a will in addition to the will substitute agreement.

9. A will substitute agreement may be useful in effectuating a basic “all to survivor” estate plan, particularly for an older couple whose estates are below the applicable exclusion amount and involve no complex assets.
10. Dispositions under a will substitute agreement are subject to disclaimer. Wis. Stat. §§ 854.01, .13. For a disclaimer to be a “qualified disclaimer” for federal gift tax purposes, the disclaimant must make the disclaimer within nine months of “the day on which the transfer creating the interest in such person is made.” I.R.C. § 2518(b)(2)(A). If, under the terms of the will substitute agreement, either spouse may unilaterally amend the provisions relating to the disposition of his or her assets, there is little doubt that the beginning date for the nine-month period is the date of the spouse’s death. The question arises, however, whether, in the case of the death of the first spouse to die, the disclaimant has nine months from the date of death when the will substitute provisions do not allow either spouse to unilaterally amend the will substitute provisions. The IRS considered this scenario in Private Letter Ruling 95-07-017 (Feb. 17, 1995), in the context of a Washington community property agreement, and concluded that “for purposes of section 2518(a)(2), the nine-month period for making the disclaimer of the decedent’s one-half community property interest passing to [surviving spouse] under the community property agreement commences on the date of death.”
11. Section 859.18(6) provides that a marital property agreement providing for the nontestamentary disposition of assets “does not affect property available under [section 859.18] for satisfaction....” It is not clear, however, how creditors’ remedies are enforced when assets completely bypass the probate estate. Note, however, that for assets passing to a trust there is a claims procedure under section 701.065, but availability to creditors depends on the procedure being initiated by the trustee to establish a claims-bar date.
12. If assets pass by nontestamentary disposition under a marital property agreement, they bypass the decedent’s estate; income attributable to those assets therefore is not taxed to the decedent’s estate, which is a separate taxpayer that may select its own fiscal year. Selection of an estate fiscal year may in some situations be advantageous to the beneficiaries. Note, however, that if the assets pass by will substitute agreement to the decedent’s revocable trust,

the trust may be able to elect pursuant to I.R.C. § 645 to have the revocable trust taxed as if part of the estate, thus allowing use of a fiscal year for a limited period of time. *See* Treas. Reg. § 1.645-1.

13. It may be preferable for some assets to be administered by a personal representative. For example, an employee-stock-option agreement may provide that, upon the death of the employee, rights under the agreement may be exercised by the deceased employee's personal representative. A comprehensive will substitute agreement transferring stock option rights without probate may result in uncertainty regarding the future exercise of stock option rights.
14. There are a number of unanswered questions concerning will substitute agreements. An agreement may be useful as part of an estate plan that is more complex than the basic all-to-survivor plan but should not be used as a complete alternative to a will. For example, it is questionable whether the decedent can direct the apportionment of federal and Wisconsin estate taxes in a will substitute agreement. The right of reimbursement for federal estate taxes paid can be waived only by a direction in a will under I.R.C. §§ 2206 and 2207, and only by the provisions of a will or revocable trust under I.R.C. §§ 2207A and 2207B.

For further discussion of the advantages and disadvantages of will substitute agreements, see chapter 7, *supra*.

In summary, a will substitute agreement, in many instances, will not be a complete substitute for a will, but it may be a valuable supplemental tool as part of the estate plan. Reliance on a will substitute agreement as the only dispositive instrument is not recommended. Coordination of the will substitute agreement with the spouses' wills and other dispositive instruments is important to coordination of the overall plan and to avoid unanticipated results.

For a more thorough discussion of nontestamentary dispositions by marital property agreement, see chapters 7 and 9, *supra*.



## VIII. Other Nonprobate Transfers at Death [§ 10.70]

### A. Payable on Death and Transfer on Death Designations [§ 10.71]

Chapter 705 authorizes forms of nonprobate transfer at death, including payable on death (P.O.D.) beneficiary designations for accounts at financial institutions and P.O.D. or transfer on death (T.O.D.) registrations for securities. *See* Wis. Stat. §§ 705.01(8), .25. Upon the death of the holder of an account or security who has made a P.O.D. or T.O.D. designation, the property passes to the designated beneficiary or beneficiaries without probate. If the account or security is classified as marital property, the surviving spouse has a remedy against the transferee to recover his or her one-half interest. *See supra* § 8.48. Failure of the surviving spouse to pursue the remedy could result in gift tax consequences for the surviving spouse. *See generally supra* ch. 9.

Spouses may believe that by making a P.O.D. or T.O.D. designation for an account or security, probate administration of the subject assets and any marital property complications will be avoided. However, if the subject assets are classified as marital property, this will not be the case if the nonholding spouse dies first.

➤ **Example.** A husband deposits \$50,000 in a bank account titled in his name alone and designates his wife as the P.O.D. beneficiary. The wife deposits \$25,000 in a bank account titled in her name alone and designates the husband as the beneficiary. All the funds are classified as marital property. If the husband dies first, the bank will be authorized to pay all the funds in his account to the wife. However, the husband's personal representative succeeds to the husband's one-half marital property interest in the wife's account, which is subject to administration.

As the example above shows, P.O.D. or T.O.D. arrangements are not particularly useful when the assets involved are classified as marital property. In some cases, however, a spouse might intentionally select such an arrangement to frustrate the efforts of the surviving spouse to claim his or her interest in marital property. The burden would then be upon the surviving spouse to pursue a remedy to enforce his or her rights. *See* chapter 8, *supra*, for a discussion of available remedies.

2005 Wisconsin Act 206, section 4, created section 705.15, which permits the nonprobate transfer of real estate via use of a P.O.D. or T.O.D. designation on a deed.

## **B. Right of Survivorship [§ 10.72]**

### **1. With Spouse [§ 10.73]**

When an asset passes by right of survivorship to the surviving spouse, the classification of the asset as marital or nonmarital property is inconsequential from the standpoint of determining the ultimate ownership of the asset. However, there are at least two reasons why one may wish to focus on the classification of the asset.

From a tax perspective, if the asset is common law joint tenancy property (as opposed to survivorship marital property), at the death of one spouse, except as noted below, only the deceased spouse's interest in the asset will receive an adjustment in basis. If the asset has a tax basis that is less than its fair market value, reclassification of the asset as marital property would be beneficial.

In some instances, an asset owned by a decedent and surviving spouse as joint tenancy property may receive a full adjustment in basis. In *Gallenstein v. United States*, 975 F.2d 286 (6th Cir. 1992), the court concluded that, when the surviving spouse had made no contribution to joint tenancy property and the joint tenancy was created before 1977, the full value of the joint tenancy property was included in the decedent's estate under the proportionate contribution rule of I.R.C. § 2040(a). Consequently, the basis of the entire property (and not just the decedent's interest) was adjusted. See also *Patten v. United States*, 1996-1 U.S.T.C. ¶60,231 (W.D. Va. 1996), *aff'd*, 116 F.3d 1029 (4th Cir. 1997); *Anderson v. United States*, 1996-2 U.S.T.C. ¶60,235 (D. Md. 1996); *Hahn v. Commissioner*, 110 T.C. 140 (1998).

From the perspective of a family-purpose creditor to whom only one spouse has incurred an obligation, a joint tenancy under section 700.17 is a more attractive form of ownership than marital property or survivorship marital property. While both spouses are living, a family-purpose creditor can reach all marital property in satisfaction of the obligation but can reach only the incurring spouse's interest in nonmarital property. See generally *supra* ch. 6. The nonincurring spouse's interest in joint

tenancy property (or tenancy in common property) is nonmarital property. Hence, it cannot be reached by a family-purpose creditor. Even if marital property funds have been mixed with joint tenancy or tenancy in common assets, the property incidents of joint tenancy or tenancy in common control. Wis. Stat. § 766.60(4)(a).

Upon the death of the only spouse who has incurred an obligation, whether property is held as joint tenancy or survivorship marital property, the property generally passes to the survivor free of claims of unsecured creditors. *See* Wis. Stat. § 859.18(4). This is not necessarily the case if the asset is a joint account under chapter 705. *See* Wis. Stat. § 705.07(2) (incorporating by reference the fraudulent transfer remedies of chapter 242 when the deceased account holder's estate is insolvent.)

## **2. With Third Party [§ 10.74]**

An asset held by one spouse with a third party in a form that includes a right of survivorship (for example, a joint tenancy or joint bank account) may be classified in part as marital property. In that event, at the death of the holding spouse, the incident of survivorship will control in the case of joint tenancy property. Wis. Stat. § 700.17(2). In the case of a joint account held by a spouse with a third party, unless there is clear and convincing evidence of a different intention at the time the account was created, the account belongs to the third party at the death of the spouse. Wis. Stat. § 705.04(1). In either case, however, the surviving spouse has a remedy against the transferee to recover his or her one-half marital property interest. *See generally supra* ch. 8. The surviving spouse's failure to pursue the remedy could result in gift tax consequences for the surviving spouse. *See generally supra* ch. 9.

In view of these complications, spouses should generally avoid holding marital property assets with a third party in a form that includes a right of survivorship. In some cases, however, a spouse might intentionally select such an arrangement to frustrate the surviving spouse's efforts to claim his or her interest in marital property assets. The burden would then be upon the surviving spouse to pursue a remedy to enforce his or her rights.

### C. Beneficiary Designations [§ 10.75]

Although federal law limits an employee's ability to designate a beneficiary other than his or her spouse in the case of qualified plans governed by ERISA, *see infra* §§ 10.134–145, a spouse having management and control of an asset that passes by beneficiary designation generally has the power to name a beneficiary to receive the asset upon death. *See* Wis. Stat. §§ 766.01(11), .51(1). If the surviving spouse is designated as the beneficiary, there is no particular concern whether the asset is classified in whole or part as marital property (note, however, that the surviving spouse's ability to disclaim all or only part of the asset is affected by the classification). If a third party is designated as the beneficiary and the asset is classified in whole or in part as marital property, the surviving spouse has a remedy against the transferee to recover his or her one-half interest. *See supra* § 8.48. The surviving spouse's failure to pursue the remedy could result in gift tax consequences for the surviving spouse. *See supra* ch. 9.

In view of these complications, it is important to consider the asset's classification when designating a beneficiary other than the surviving spouse for an asset that passes by beneficiary designation. If the asset is classified as marital property and a third party is an intended beneficiary, the beneficiary designation can include a direction to pay the surviving spouse's marital property interest to him or her, with the balance passing to the third-party beneficiary. If a trust is designated as the beneficiary, the terms of the trust can include a provision directing that the surviving spouse's interest in former marital property be distributed to him or her or to a trust that he or she controls. For example, if the spouses have created a joint revocable living trust designed to hold marital property and the trust is designated as the beneficiary of a life insurance policy classified as marital property, the provisions of the trust would provide for allocation of the surviving spouse's marital property interest to him or her or to a survivor's trust (which is revocable by the survivor).

In some cases, a spouse might intentionally designate a third party as beneficiary of a marital property asset to frustrate the surviving spouse's efforts to claim his or her interest in the asset. The burden would then be upon the surviving spouse to pursue a remedy to enforce his or her rights. *See* chapter 8, *supra*, for a discussion of available remedies.

## D. Other Nonprobate Transfers [§ 10.76]

Section 705.10, entitled “Nonprobate transfers at death,” enumerates a panoply of methods that can be used to transfer property at death without a will. In pertinent part, it provides:

A provision for a nonprobate transfer on death in an insurance policy, contract of employment, bond, mortgage, promissory note, certificated or uncertificated security, account agreement, custodial agreement, deposit agreement, compensation plan, pension plan, individual retirement plan, employee benefit plan, trust, conveyance, deed of gift, marital property agreement, or other written instrument of a similar nature is nontestamentary.

Wis. Stat. § 705.10(1). The section goes on to list the types of property that can be transferred by such means, including “[a]ny property controlled by or owned by the decedent before death which is the subject of the instrument passes to a person whom the decedent designates either in the instrument or in a separate writing, including a will executed either before or at the same time as the instrument, or later.” Wis. Stat. § 705.10(1)(c). Creditors’ rights are not compromised by the use of a nonprobate transfer under section 705.20. Wis. Stat. § 705.10(2). By virtue of an amendment made by 1997 Wisconsin Act 188 (making major changes to Wisconsin’s probate code), section 705.20 is tied into the probate code by its cross reference to chapter 854. Wis. Stat. § 705.10(3).

The Wisconsin Court of Appeals cited section 705.20 (the predecessor to 705.10) as authority for its holding in *Reichel v. Jung (In re Estate of Jung)*, 2000 WI App 151, 237 Wis. 2d 853, 616 N.W.2d 118, discussed in section 10.33, *supra*, regarding the transfer of an annuity at death pursuant to its contract terms. Given its breadth, section 705.10 may have other applications that have yet to be tested in court. For example, by its terms, section 705.10 would seem to authorize the titling of real property in a manner such that it can be owned by one person during his or her life and then pass to another at the owner’s death pursuant to the terms of the governing instrument.

2005 Wisconsin Act 206, section 5, which renumbered section 705.20 as section 705.10 added a new subsection (4), expanding the manner in which a nonprobate transfer can be confirmed following death. Both 2005 Wisconsin Acts 206 and 216 contain provisions expanding the

manner in which nonprobate transfers can be confirmed under section 867.046. *Cf. Maciolek v. City of Milwaukee Employees' Ret. Sys. Annuity & Pension Bd.*, 2006 WI 10, 288 Wis. 2d 62, 709 N.W.2d 360. For greater detail on the connection between *Maciolek* and these changes, see sections 12.173 and .174, *infra*.

## **IX. Lifetime Gifts [§ 10.77]**

### **A. In General [§ 10.78]**

Lifetime gifts of property can be an important part of the estate planning process. Such gifts may be used to take advantage of the annual exclusion from federal gift or generation-skipping transfer taxes or may be part of more sophisticated planning techniques to transfer value to descendants. A number of these techniques and the specific concerns relating to transfers in a marital property regime are considered in Part XI of this chapter, *supra*. Following is a discussion of the basic issues involved in making lifetime gifts of marital and nonmarital property assets.

### **B. Gifts of Individual Property Assets [§ 10.79]**

Under section 766.51(1), a spouse acting alone may manage and control his or her nonmarital property, which includes that spouse's individual property assets. *Management* and *control* are defined broadly in section 766.01(11) to allow the party having management and control to deal with property as if it were the property of an unmarried person. The duty of good faith applicable to dealings with respect to marital property or nonmarital property of the other spouse is not applicable to a spouse's own individual property. *See* Wis. Stat. § 766.15.

Hence, a spouse is generally free to make gratuitous transfers of his or her own individual property during lifetime, with some limited exceptions. Section 766.51(8) preserves section 706.02(1)(f)'s requirement that a spouse join in a conveyance of an interest in homestead property, other than the granting of a purchase money mortgage. Note, however, that a valid waiver of homestead rights in a marital property agreement eliminates the need for the nontitled spouse's signature. *See Jones v. Estate of Jones*, 2002 WI 61, 253 Wis. 2d 158, 646 N.W.2d 280. Federal law limits a spouse's ability to alienate an

interest in an ERISA-qualified plan, even though it may be classified under state law as individual property. *See infra* §§10.134–.146. A spouse's beneficial interest in a trust created by a third party, although classified as that spouse's individual property, may nonetheless be subject to limitations on transfer by the terms of the trust (e.g., a spendthrift clause). A spouse who has been divorced may be subject to limitations on the transfer of property (including his or her individual property assets) under the provisions of a divorce judgment designed to protect the support rights of the former spouse or children. Though they do not restrict the power to make transfers in the first instance, fraudulent transfer remedies under state law or federal bankruptcy law can result in the avoidance of a gratuitous transfer of a spouse's individual property assets if the transfer was made in actual or constructive fraud of a creditor's rights. It is also possible, though unlikely, that a transfer of individual property assets during lifetime could give rise to an equitable remedy under section 861.17, as discussed in section 10.80, *infra*.

If an individual property asset is the subject of a gift, unless the gift is to the other spouse, the spouses may elect to treat the gift as having been made one-half by each spouse for federal gift tax purposes. *See* I.R.C. § 2513. By contrast, if the subject of a gift is a marital property asset, the gift is deemed to have been made one-half by each spouse, such that the election under I.R.C. § 2513 is unnecessary. *See supra* ch. 9.

### **C. Gifts of Predetermination Date Property Assets** **[§ 10.80]**

The considerations with respect to gifts of predetermination date property assets are the same as those with respect to gifts of individual property assets, with two additional considerations in the case of assets meeting the definition of deferred marital property under section 851.055. (For predetermination date property assets meeting the definition of deferred individual property under section 861.018(2), the considerations are identical to those applicable to gifts of individual property assets.)

If deferred marital property assets are given away within two years of the donor's death or if the donor transfers such assets and retains certain rights in the transferred property, the assets may be included within the deferred marital property election available to the surviving spouse and

may be subject to recovery. *See* Wis. Stat. §§ 861.03(3), (4), .06(4); *see also infra* ch. 12.

In addition, section 861.17 provides a general equitable remedy for the surviving spouse in the event of property arrangements made by the decedent in fraud of the survivor's rights under chapter 852 (governing intestate succession) and chapter 861 (which includes not only deferred marital property elective rights under section 861.02, but other family rights relating to homestead property, selection of personalty, family allowance, etc.; *see* Wis. Stat. §§ 861.21–.35).

## **D. Gifts of Marital Property Assets [§ 10.81]**

### **1. Power to Make Gifts; Limitations; Remedies [§ 10.82]**

Because the right to manage and control marital property assets specifically includes the power to make gifts, Wis. Stat. § 766.51(4), a gift of a marital property asset is complete when made even though it may be subject to a remedy pursuant to section 766.53. *See supra* ch. 9. For a discussion of the right to make gifts of marital property assets pursuant to the power of management and control, *see* chapter 4, *supra*. For a discussion of remedies in the case of gifts of marital property assets, *see* generally chapter 8, *supra*.

### **2. Donor or Transferor for Federal Transfer Tax Purposes [§ 10.83]**

Because each spouse owns an undivided one-half interest in each item of marital property, *see* Wis. Stat. § 766.31(3), a gift of a marital property asset, even if effected by the unilateral act of only one spouse (when that spouse has management and control under section 766.51(1)), is deemed for federal transfer tax purposes to have been made one-half by each of the spouses. *See supra* ch. 9.

Thus, for federal gift tax purposes, each spouse is deemed to have made a gift of one-half of a marital property asset, thereby making the filing of a gift-splitting election pursuant to I.R.C. § 2513 unnecessary for marital property assets.



➤ **Example.** A wife holds title to a bank account funded with earnings from her employment. She gives a check in the amount of \$22,000 drawn on the account to her niece as a gift. Neither the husband nor the wife make any other gifts to the niece during the calendar year. Since the funds are classified as marital property, gifts during the calendar year to the niece from the husband and wife are limited to \$11,000 per donor. No gift tax return is required with respect to the \$22,000 given to the niece.

By contrast, if the funds in the wife's savings account were nonmarital property, for the \$22,000 gift to the wife's niece to qualify for the gift tax annual exclusion, the wife and the husband would need to make an election under I.R.C. § 2513 to have gifts made by them during the calendar year treated as having been made one-half by each.

The "transferor" for GST tax purposes under I.R.C. ch. 13 is deemed to be the same as the donor for gift tax purposes under I.R.C. ch. 12. I.R.C. § 2652(a). Split gifts for gift tax purposes under I.R.C. § 2513 are so treated for GST purposes under I.R.C. ch. 13. *Id.* Hence, if a marital property asset is the subject of a GST under I.R.C. ch. 13, each spouse will be regarded as a transferor of one-half of the asset for GST tax purposes. If a transferred asset is not classified as marital property, to achieve the same result the spouses must make a gift-splitting election under I.R.C. § 2513.

The treatment of a marital property asset gratuitously transferred during lifetime by one spouse as having been given one-half by each spouse carries through for federal estate tax purposes. This can have adverse estate tax effects. See chapter 9, *supra*, for a discussion of I.R.C. § 2036 issues that may arise when marital property assets have been the subject of a gift and the surviving spouse has a retained interest.

## **X. Marital Deduction/Credit Shelter Planning [§ 10.84]**

### **A. Use of Marital Property Classification to Balance Estates [§ 10.85]**

Classic estate planning for spouses includes using the unlimited estate tax marital deduction under I.R.C. § 2056 and the applicable credit amount under I.R.C. § 2010 to eliminate estate tax in the estate of the

first spouse to die and to reduce (or eliminate) estate tax in the survivor's estate. The ability to easily equalize the sizes of the spouses' respective estates with a marital property agreement can facilitate estate tax planning in two important ways.

First, when the spouses' assets are classified as marital property, each spouse owns an undivided one-half interest in each marital property asset and has the power of testamentary disposition at death with respect to his or her one-half interest, subject to the terminable interest rule applicable to deferred employment benefits and some IRAs. This is important for making use of the applicable credit amount when the first spouse dies, because if the spouses' estates are grossly unequal and the spouse with fewer assets dies first, a portion of the applicable credit amount may be wasted.

Second, the estate tax rates prescribed by I.R.C. § 2001 are graduated. If the spouses' combined estates exceed twice the amount that may be sheltered from estate tax by the applicable credit amount, overall estate tax savings can be achieved by equalizing the spouses' estates and paying estate tax in the first estate to utilize the lower marginal tax brackets (in contrast to deferring all estate tax to the survivor's estate, in which case the tax on amounts that qualified for the estate tax marital deduction in the first estate will be at higher marginal rates). Given the uncertainty as to which spouse will die first, balancing the size of the spouses' respective estates with a marital property agreement places the spouses in the best position to use this tax-savings strategy, whether the focus is on minimizing federal estate taxes, Wisconsin estate taxes, or both.

## **B. Use of QTIP Marital Trust to Facilitate Valuation Discount [§ 10.86]**

One decision in implementing a marital deduction/credit shelter plan is deciding whether assets qualifying for the marital deduction in the first spouse's estate should pass to a qualified terminable interest property trust (QTIP trust) or outright to the survivor (or to a power-of-appointment marital trust). In the case of closely held business interests classified as marital property when the spouses together hold a majority interest, the use of a QTIP trust may facilitate valuation discounts in the survivor's estate.

➤ **Example.** A wife and her husband own, as marital property, 80% of the stock of a corporation. The wife dies first and leaves her one-half interest (40% of the stock of the corporation) to a QTIP trust for the husband's benefit. Upon the husband's later death, his 40% of the stock and the QTIP trust's 40% of the stock are includible in his gross estate for federal estate tax purposes. On the federal estate tax return filed in the husband's estate, the stock owned by the QTIP trust and the stock owned by the husband's estate are valued as separate 40% minority interests, rather than together as an 80% controlling interest.

See *Estate of Bonner v. United States*, 84 F.3d 196 (5th Cir. 1996), and *Estate of Mellinger v. Commissioner*, 112 T.C. 4 (1999), discussed in section 10.121, *infra*. Hence, the use of a QTIP trust as the recipient of the decedent's one-half marital property interest in a closely held business interest can reduce the value of the survivor's gross estate for federal estate tax purposes, thereby reducing estate taxes.

## **XI. Planning Considerations for Specific Types of Property [§ 10.87]**

### **A. Jointly Held Assets and Forms of Holding Title [§ 10.88]**

#### **1. In General [§ 10.89]**

Spouses often hold assets in a joint form that gives them equal rights of management and control. A joint form of holding title to assets also may include a right of survivorship (e.g., a joint bank account or survivorship marital property). In some cases, a right of survivorship may be desirable; in others, it may not (e.g., when, for estate tax planning purposes, each spouse needs to have a power of disposition over an asset at death to make full use of the applicable credit amount).

As indicated below, the various forms of holding title for different classifications of property vary depending on the type of asset involved.

## 2. Wisconsin Real Estate [§ 10.90]

Spouses may hold title to Wisconsin real estate classified as marital property in one of the following eight forms:

1. In the husband's name alone;
2. In the wife's name alone;
3. In the spouses' names together either in the "and" form or in the "or" form "as marital property," *see* Wis. Stat. § 766.60(1), (2);
4. In the spouses' names together as "tenants in common," deemed by section 766.60(4)(b)1.b. to constitute marital property if established after the spouses' determination date, unless otherwise provided in a marital property agreement;
5. In the spouses' names together as "joint tenants," deemed by section 766.60(4)(b)1.a. to constitute survivorship marital property if established after the spouses' determination date, unless otherwise provided in a marital property agreement;
6. In the spouses' names together either in the "and" form or in the "or" form "as survivorship marital property," *see* Wis. Stat. § 766.60(5)(a);
7. In the spouses' names together without designation or simply designated as "husband and wife"; and
8. In the name of one or both spouses or a third party as trustee(s) of a revocable trust that is designed to hold marital property assets.

If the property is acquired exclusively by the spouses after the determination date and is the spouses' homestead, the property is survivorship marital property, absent a contrary intent expressed in the instrument of transfer or in a marital property agreement. Wis. Stat. § 766.605.

The form selected for holding title to real estate may depend on the spouses' wishes regarding management and control, rights of survivorship, avoidance of probate of the subject real estate, or limiting exposure of the property to the creditors of one spouse. Whether to

include or exclude a right of survivorship may be dictated by the type of estate tax planning adopted (for example, marital deduction/credit shelter planning) or by each spouse's wishes regarding the disposition of his or her interest to someone other than the survivor (for example, to his or her children from a prior marriage).

In some instances spouses may choose to convert their interests in real estate classified as marital property (either with or without right of survivorship) into a form of personalty that affords limited liability, such as a limited liability company (LLC) or limited liability partnership (LLP). In that case, the LLC membership interest or LLP partnership interest will be classified as marital property, and the incidents of survivorship will depend on the form of holding title to the interest (or, if applicable, by the terms of a marital property agreement).

If Wisconsin real estate was acquired before the spouses' determination date, its classification as of the determination date is determined under chapter 700, and in particular sections 700.17 through 700.20 with respect to concurrent interests (joint tenancy and tenancy in common). However, postdetermination date events, such as asset or labor mixing or entering into a marital property agreement, can alter the classification in whole or in part. See chapter 3, *supra*, for a discussion of mixing and tracing, and sections 10.18–.33, *supra*, regarding the effect of a marital property agreement on the classification of predetermination date joint tenancy property. See sections 10.171–.177, *infra* and chapter 6, *supra*, regarding creditors' rights issues to consider in deciding whether to reclassify predetermination date property as marital property.

### **3. Bank Accounts [§ 10.91]**

In this section the term *bank account* is used as shorthand to refer to an account at a *financial institution*, as that term is defined in section 705.01(3). The term financial institution arguably does not include brokerage firms, since the statutes treat accounts under section 705.01(1) and brokerage accounts as separate. See Wis. Stat. § 766.01(9)(b); *but see* § 10.32, *supra* (discussing *Templeton v. Moccero (In re Estate of Moccero)*, 168 Wis. 2d 313, 321, 483 N.W.2d 310 (Ct. App. 1992) (equating joint brokerage account with *account* under chapter 705)).

Chapter 705 authorizes essentially two types of bank accounts that spouses may hold jointly: joint accounts and marital accounts. See Wis.

Stat. § 705.02(1)(a), (d). In addition, a P.O.D. feature may be added to either type of account. *See* Wis. Stat. § 705.02(1)(c), (e). *See* section 10.71, *supra*, for a discussion of P.O.D. accounts holding marital property funds. Although joint accounts may be owned by multiple parties who are not married to one another and include a presumptive right of survivorship, *see* Wis. Stat. § 705.04(1), marital accounts may be owned only by a husband and wife and do not include a right of survivorship (although this may be altered by a marital property agreement), *see* Wis. Stat. § 705.04(2m). Absent a contrary provision in a marital property agreement, 50% of the amount remaining in a marital account may be withdrawn by the survivor upon the death of a spouse and the other 50% may be withdrawn by the decedent's estate. *Id.* Alternatively, it appears that a P.O.D. designation may be used with respect to disposition of the interest of a deceased spouse in a marital account. *See* Wis. Stat. § 705.06(1)(d).

Thus, in some respects a joint account held by spouses is analogous to joint tenancy property or survivorship marital property, since the sums in the account pass to the survivor upon the death of a spouse, at least presumptively. Likewise, in some respects a marital account held by spouses is analogous to tenancy in common property or marital property, since one-half remains with the survivor and the other half is subject to testamentary disposition in the decedent's estate.

The choice between a marital account and a joint account, therefore, depends on whether a right of survivorship is desired as part of the spouses' estate plan. The extent to which a provision in a marital property agreement classifying assets as marital property may affect the presumptive right of survivorship for a joint account is discussed at section 10.32, *supra*.

If spouses have created a joint revocable trust designed to hold marital and nonmarital property assets as part of their estate plan, a bank account may be held by the spouses as trustees of the trust. At the death of one spouse, the terms of the trust will specify the disposition of the sums remaining in the account.

A spouse who wants to preserve the classification of funds as individual property and avoid controversy such as that which arose in *Lloyd v. Lloyd (In re Estate of Lloyd)*, 170 Wis. 2d 240, 487 N.W.2d 647 (Ct. App. 1992), discussed at section 3.14, *supra*, should avoid placing them in either a joint account or a marital account with his or her spouse.

#### 4. Securities Held Directly [§ 10.92]

Securities held directly by one or both spouses (as opposed to in a brokerage account) may be held in a number of different forms. If the securities are those of a closely held company, permissible forms of holding may include forms unique to Wisconsin law (e.g., “Husband or Wife as marital property,” “Husband and Wife as survivorship marital property,” or “Husband [or Wife] as individual property”). *See* Wis. Stat. § 766.60.

If the securities are registered, however, a transfer agent likely will not recognize these unique forms of holding title under Wisconsin law. Instead, securities classified as marital property without right of survivorship likely will be titled in one of four ways: (1) in the name of the husband alone; (2) in the name of the wife alone; (3) in the names of the husband and wife as “tenants in common,” deemed by section 766.60(4)(b)1.b. to constitute marital property if established after the spouses’ determination date; or (4) in the name of one or both spouses or a third party as trustee(s) of a revocable trust that is designed to hold marital property assets. The option selected will depend on the spouses’ wishes regarding management and control and their interest in avoiding probate of the securities. Any of the above four forms of holding title can be used as a means to enable the first spouse to die to direct the disposition of his or her one-half interest, which is important in marital deduction/credit shelter planning. For a discussion of marital deduction/credit shelter planning, see sections 10.84–.86, *supra*.

If the spouses wish to hold the securities in a form that includes a right of survivorship, they may take title in the form “Husband and Wife as joint tenants,” which, if established after the spouses’ determination date, will cause the securities to be owned as survivorship marital property (absent a contrary provision in a marital property agreement). *See* Wis. Stat. § 766.60(4)(b)1.a. The same result can be achieved by holding title in the name of a revocable trust if the terms of the trust provide that upon the death of the first spouse, the survivor becomes the sole beneficiary of the trust with a continuing power of revocation. This arrangement may be appropriate when estate tax planning is unnecessary and the spouses want to avoid probate at both deaths.

If securities are the nonmarital property of one spouse, that spouse may hold title to the security in his or her name alone or in the name of a trustee or trustees of a revocable trust created by that spouse. If the

estate plan adopted by the spouses includes a joint revocable trust designed to hold both marital property assets and nonmarital property assets, a security may be held in the name of the trustees of such trust, in which case either the form of holding or the trustees' records should reflect that the security is held as nonmarital property (for example: "Husband and Wife, as Trustees of the Husband and Wife Living Trust (Husband nonmarital account)").

Subchapter III of chapter 705 authorizes the registration of securities in beneficiary form by using a P.O.D. or T.O.D. designation. For a discussion of P.O.D. and T.O.D. designations, see section 10.71, *supra*.

For a discussion of the effect of a marital property agreement on the classification of, or the right of survivorship with respect to, securities registered in the names of spouses as joint tenants, see section 10.31, *supra*.

## **5. Brokerage Accounts and Mutual Funds [§ 10.93]**

The alternative forms of holding title to a brokerage account or mutual fund account will depend on the options afforded by the particular brokerage firm or mutual fund company. For example, the Vanguard Group mutual fund company has offered four different forms of co-ownership registration, including "joint tenants with right of survivorship," "tenants in common," "tenants by the entirety" (available only to married persons), and "community property" (available only to married persons residing in one of the nine community property states). Because incidents of survivorship vary depending on the type of account used, the most straightforward approach in selecting a form of holding title is to choose a form consistent with the spouses' intent regarding incidents of survivorship.

Hence, if the desire is for an account to be owned as marital property without right of survivorship, for any brokerage account or mutual fund account there should be at least four options, as follows: (1) in the name of the husband alone; (2) in the name of the wife alone; (3) in the names of the husband and wife as "tenants in common," deemed by section 766.60(4)(b)1 to constitute marital property if established after the spouses' determination date; or (4) in the name of one or both spouses or a third party as trustee(s) of a revocable trust that is designed to hold marital property assets. In addition, if the particular brokerage firm or



mutual fund company offers the option, an account may be held as “marital property” or as “community property.” As to the latter form of holding, it should be noted that chapter 766 does not per se recognize “community property” as a form of holding marital property assets. However, section 766.001(2) states the legislature’s intent that marital property be regarded as “a form of community property.” Hence, an account held by Wisconsin-domiciled spouses as “community property” should be regarded as marital property under chapter 766 (any uncertainty regarding this conclusion could be eliminated by a provision in a marital property agreement stating that any assets held as community property are classified as marital property). The choice selected for the form of holding title may depend on the spouses’ wishes regarding management and control, rights of survivorship, avoidance of probate, or limiting exposure of the property to the creditors of one spouse. Any of the forms of holding title can be used to enable the first spouse to die to direct the disposition of his or her one-half interest, which is important in marital deduction/credit shelter planning. For a discussion of marital deduction/credit shelter planning, see sections 10.84–.86, *supra*.

If the spouses wish to hold a brokerage account or mutual fund account in a form that includes a right of survivorship, they may establish a “joint tenants with right of survivorship account” or its equivalent. If established after the spouses’ determination date, this form of holding causes the account to be owned as survivorship marital property (absent a contrary provision in a marital property agreement). *See* Wis. Stat. § 766.60(4)(b)1.a. The same result can be achieved by holding title in the name of a revocable trust in which the terms of the trust provide that, upon the death of the first spouse, the survivor becomes the sole beneficiary of the trust with a continuing power of revocation. Such arrangement may be appropriate when estate tax planning is unnecessary and the spouses want to avoid probate at both deaths.

If a brokerage account or mutual fund account is the nonmarital property of one spouse, that spouse may hold title to the account in his or her name alone or in the name of a trustee or trustees of a revocable trust created by that spouse. If the estate plan adopted by the spouses includes a joint revocable trust designed to hold both marital property assets and nonmarital property assets, an account may be held in the name of the trustees of such trust, in which case either the form of holding or the trustees’ records should reflect that the account is held as nonmarital

property (for example: “Husband and Wife, as Trustees of the Husband and Wife Living Trust (Husband nonmarital account”).

Subchapter III of chapter 705 authorizes the registration of a “security” (which includes a security account, Wis. Stat. § 705.21(11)) in beneficiary form by using a P.O.D. or T.O.D. designation. For a discussion of considerations related to the use of P.O.D. and T.O.D. designations, see section 10.71, *supra*. Although subchapter III of chapter 705 includes provisions that may be applicable to brokerage accounts or mutual fund accounts, subchapter I of chapter 705, dealing with multiparty and agency accounts, is limited in application to “financial institutions,” which does not include brokerage firms or mutual fund companies, as the statutes treat accounts under section 705.01(1) and brokerage accounts as separate. See Wis. Stat. § 766.01(9)(b), *but see supra* § 10.32 (discussing *Estate of Moccero*, 168 Wis. 2d at 321, in which the court equated a joint brokerage account with an account under chapter 705).

For a discussion of the effect of a marital property agreement on the classification of, or the right of survivorship with respect to, a brokerage account held by spouses jointly, see section 10.32, *supra*.

## **B. Tangible Personal Property [§ 10.94]**

During a marriage spouses may accumulate significant amounts of tangible personal property, which can range in value from ordinary (such as clothing or appliances) to extraordinary (for example, valuable antiques or items of jewelry). Like all property of married persons domiciled in Wisconsin, items of tangible personal property are presumed to be marital property, Wis. Stat. § 766.31(2), and in most cases will be so classified unless they were received by one spouse by gift or transfer at death, *see* Wis. Stat. § 766.31(7)(a), are traceable to acquisition with nonmarital property funds, or are classified otherwise by a marital property agreement.

Because application of the item-by-item rule, *see supra* § 10.10, will require that one-half of each marital property asset be subject to administration at the death of the first spouse (unless subject to some nonprobate form of transfer), spouses may wish to simplify matters by excluding certain categories of tangible personal property from classification as marital property (e.g., personal effects) or by specifying

that other kinds of tangible personal property are survivorship marital property (e.g., household furniture and furnishings). If one spouse wishes to leave a particular item to someone other than his or her spouse, that item should be classified as that spouse's individual property.

See also section 10.10, *supra*, describing the option of deviating from the item-by-item rule by virtue of the change made to section 766.31(3) by 2005 Wisconsin Act 216, section 42.

### **C. Income in Respect of a Decedent (IRD) Items** **[§ 10.95]**

Income in respect of a decedent (IRD) items, such as U.S. savings bonds, IRAs, or deferred compensation arrangements (to name just a few) may be marital, nonmarital, or mixed property. Regardless of classification, however, IRD items are not eligible for an adjustment in basis upon the death of the owner. I.R.C. § 1014(c); *see supra* ch. 9. Moreover, IRD items generally are a poor choice for funding a credit shelter trust since some of the deceased spouse's applicable credit amount is "wasted" by the payment of income tax from the credit shelter trust. Even if classified as marital property, many IRD items are subject to the terminable interest rule under sections 766.31(3) and 766.62(5) such that, upon the death of the nonemployee spouse, the marital property interest of the nonemployee spouse terminates. Further, if the IRD item is an ERISA-qualified plan governed by the Retirement Equity Act, a predeceasing spouse has no power to make a testamentary disposition of his or her marital property interest in the plan.

Hence, there is generally little tax advantage to having an IRD item classified as marital property. Indeed, in some cases there may be a disadvantage; if the noncontracting spouse dies first, and his or her will makes a testamentary disposition of a one-half interest in the IRD item, the administration of the estate will be unnecessarily complicated.

➤ **Example.** A wife's non-rollover IRA is attributable entirely to contributions of marital property assets. Her husband dies first, leaving his residuary estate to a trust. Following the husband's death, the wife makes additional contributions to her IRA.

In this example, the husband's will is effective to transfer his one-half marital property interest in the wife's IRA to the trust. The husband's interest in the IRA should be inventoried as part of his estate, but access to the IRA assets may be deferred until distributions are made from the IRA since management and control of the IRA is with the surviving wife. To protect the estate's interest, the husband's personal representative would be well advised to obtain an order from the probate court declaring the estate's proportionate interest in future distributions from the wife's IRA. The wife's additional contributions to the IRA following the husband's death illustrate the complexity that can result in the absence of careful planning. The wife should avoid making additional contributions to the same IRA account following the husband's death and should instead make future IRA contributions to a separate account to avoid commingling.

The spouses in the example above could have prevented the testamentary disposition of the husband's marital property interest by including a provision in a marital property agreement that affirmatively applies the terminable interest rule to the wife's IRA. Similarly, by marital property agreement the spouses may agree to the application of the terminable interest rule to other types of IRD items.

For specific discussions of planning for various types of IRD items, see sections 10.96 (savings bonds), 10.98 (annuities), 10.99 (stock options), 10.132–.147 (deferred employment benefits), and 10.148–.160 (IRAs), *infra*.

#### **D. U.S. Savings Bonds [§ 10.96]**

Because the accrued interest in U.S. savings bonds is an element of income in respect of a decedent, there is no adjustment in the basis of savings bonds upon death. *See* I.R.C. § 1014(c). Hence, classifying savings bonds as marital property will not achieve the same potential income tax benefit as classifying capital assets as marital property.

Savings bonds may be registered in joint or P.O.D. beneficiary form. *See* 31 C.F.R. §§ 353.7 (Series EE and HH bonds); 31 C.F.R. § 360.6 (Series I bonds). If bonds are held in joint form by spouses, the surviving spouse succeeds to ownership upon the death of the other spouse, and classification is irrelevant. Likewise, if the holding spouse

dies first and the survivor is the P.O.D. beneficiary, the survivor succeeds to ownership and the classification is irrelevant.

If the nonholding spouse dies first and the bonds are classified as marital property, as with any other asset classified as marital property, the decedent's personal representative succeeds to the ownership interest of the deceased spouse and may seek the assistance of the probate court in exercising management and control rights or obtaining the retitling of the bonds. *See* Wis. Stat. § 857.01.

If a savings bond is classified in whole or in part as marital property and is held by a spouse with a third party in joint form or with a third party named as P.O.D. beneficiary, federal regulations govern the succession of ownership of the bond upon the death of the holding spouse. *See supra* ch. 2. Notwithstanding the force of federal regulations, a successor owner may be required to account to the surviving spouse with respect to the survivor's marital property interest. *Id.*

## **E. Life Insurance [§ 10.97]**

Chapter 766 provides special classification rules for certain life insurance policies under section 766.61. In some instances application of these rules makes it difficult to determine the classification of a policy and its proceeds. For example, if a policy insuring the life of one spouse under which that spouse is the designated owner was acquired before the spouses' determination date and marital property assets were used to pay at least one premium on the policy after the determination date, the ownership interest and proceeds of the policy are mixed property. Wis. Stat. § 766.61(3)(b). The determination of the marital property component requires an investigation of records of policy issuance and premium payments. From a planning standpoint, the application of these mixing rules can be avoided by classifying the policy as either marital property or individual property. If the spouses are entering into a marital property agreement, they can include a provision classifying life insurance policies. In some instances, however, it may be preferable to use a written consent if the spouses decide to classify a policy as the individual property of one spouse.

Whether a life insurance policy should be classified as marital property or individual property will depend on the facts in the particular

case. If the insured spouse is the designated owner and the spouses do not reclassify the policy, the policy will typically be marital property from the outset, *see* Wis. Stat. § 766.61(3)(a), or will acquire a significant marital property component over time, *see* Wis. Stat. § 766.61(3)(b), depending when the policy was issued relative to the spouses' determination date. Since life insurance can be a useful means of funding a credit shelter trust, the classification of a policy as the individual property of the insured provides the ability to effectively use 100% of the proceeds to fund the credit shelter trust if the insured spouse dies first. If the same policy were instead classified as marital property, only the decedent's one-half interest in the proceeds could be used to fund the credit shelter trust, since the survivor would have a claim of ownership to the other half, *see* Wis. Stat. §§ 766.61(2), .70(6)(b), and allowing all of the proceeds to pass to the credit shelter trust would result in the estate tax inclusion of a portion of the trust in the survivor's estate under I.R.C. § 2036(a). *See supra* ch. 9.

On the other hand, reclassifying a policy of life insurance as individual property may deprive the noninsured spouse of valuable property rights. Hence, the planner (particularly in a joint representation) may wish to consult with the spouses regarding the relative advantages and disadvantages of the proposed classification. In some cases (particularly when sufficient assets exist to fund the credit shelter trust by other means), the better course may be to provide for the classification of a policy as marital property so that each spouse continues to have an ownership interest in the policy and proceeds.

When a life insurance policy is classified as marital property, a further question for the planner is whether to override the so-called *frozen interest rule* under section 766.61(7). For a discussion of the frozen interest rule, *see* chapters 2 and 7, *supra*. Under the rule, absent an express provision in a marital property agreement to the contrary, the interest of the estate of a predeceasing noninsured spouse in the marital property component of a policy insuring the life of the survivor is limited to a dollar amount; the estate does not succeed to a one-half interest in the policy itself. The purpose of the frozen interest rule is to prevent the inadvertent disposition of a marital property interest in life insurance if the noninsured spouse predeceases the insured spouse.

Spouses may override the frozen interest rule by express provision in a marital property agreement. Wis. Stat. § 766.58(7)(b). There are circumstances in which it could be beneficial to classify a life insurance

policy as marital property with the frozen interest rule overridden. For example, the noninsured spouse may wish to utilize his or her unified credit or make a disposition to a child from a previous marriage. If the spouses classify the life insurance policy as marital property and override the frozen interest rule, the noninsured spouse can provide for a disposition of his or her marital property interest in the life insurance to a third person such as a child or a credit shelter trust. If the noninsured spouse wishes to make a disposition to a trust, the insured spouse should not have incidents of ownership over the life insurance as a fiduciary or beneficiary. *See* Rev. Rul. 84-179, 1984-2 C.B. 195.

Generally, if life insurance is classified as marital property and the insured spouse is the first to die, one-half of the value of the policy will be included in the insured's estate for federal estate tax purposes. However, if the insured transferred an interest in the policy to the noninsured spouse within the three-year period before the insured's death, the insured's proportionate interest at the date of transfer will be included in the insured's estate for federal estate tax purposes. I.R.C. § 2035; *see supra* ch. 9.

If life insurance under which a spouse is the insured is owned by a corporation, the classification of stock of the corporation as marital property may avoid the estate tax inclusion of life insurance proceeds under the controlling stockholder rule of Treas. Reg. § 20.2042-1(b)(6). Under the regulation, the proceeds of a life insurance policy owned by a corporation on the life of the controlling stockholder are includible in the deceased controlling stockholder's estate. A decedent is deemed a controlling stockholder if at death he or she owned stock possessing more than 50% of the total combined voting power of the corporation. The recognition of the noncontrolling status of a decedent's one-half community property interest in other contexts should apply for purposes of Treas. Reg. § 20.2042-1(b)(6) as well. *See, e.g., Estate of Lee v. Commissioner*, 69 T.C. 860 (1978), *nonacq.*, 1980-1 C.B. 2, *nonacq. withdrawn and acq. substituted*, 1993-1 C.B. 202 (treating decedent's community property interest in 80% of stock of corporation as 40% minority interest); *Propstra v. United States*, 680 F.2d 1248 (9th Cir. 1982) (allowing discount in valuing decedent's one-half community property interest in real estate); *Estate of Bright v. United States*, 658 F.2d 999 (5th Cir. 1981) (rejecting family attribution and treating decedent's community property interest in 55% of a company's outstanding stock as a 27.5% minority interest); Rev. Rul. 93-12, 1993-1 C.B. 202 (rejecting aggregation of family interests in shares with

transferred shares for purposes of determining whether transferred shares should be treated as a controlling interest).

For a discussion of planning considerations for life insurance held in an irrevocable life insurance trust, see section 10.117, *infra*.

## **F. Annuities [§ 10.98]**

Chapter 766 provides no special classification rules for annuities, which it does for certain life insurance policies and deferred employment benefits (*see supra* ch. 2). Hence, the general classification rules under section 766.31 apply to annuities; however, the classification of an annuity provided as a deferred employment benefit is governed by the special classification rules under section 766.62.

An annuity policy typically permits the person designated as the owner of the policy to designate a beneficiary for any proceeds payable upon death. If the nonowner spouse survives and is designated as the beneficiary, the classification of the annuity is of little concern. If the nonowner spouse survives and is not designated as the beneficiary, the classification of a portion or all of the annuity policy as marital property will give rise to a remedy by the surviving spouse for his or her one-half interest in the marital property component. *See* Wis. Stat. § 766.70.

Unless an annuity is provided as a deferred employment benefit, the terminable interest rule under sections 766.31(3) and 766.62(5) will not apply to any portion of the annuity classified as marital property. Hence, if the nonowner spouse dies first, one-half of the marital property component of the annuity is subject to testamentary disposition by the decedent. This may be an undesirable result given the complexity of classifying the annuity and determining the portion of any annuity payments due the estate of the nonowner. Spouses wishing to avoid this result have essentially two options. First, the spouses can agree in a marital property agreement that the annuity is the individual property of the designated owner. The death of the nonowner will have no effect on the owner's continued rights in the policy. However, if the annuity was acquired with marital property assets, by classifying the annuity as individual property, the nonowner spouse has given up the right to claim a remedy if he or she survives and is not named as the beneficiary. The other option is for the spouses to allow the annuity to be classified as provided under chapter 766 but to specify in a marital property



agreement that the terminable interest rule will apply in the same manner as it would to a deferred employment benefit. In this manner, the surviving nonowner does not give up his or her rights in the annuity, but the predeceasing nonowner has no power of testamentary disposition.

Although investment decisions regarding annuities often do not involve the estate planner, if the opportunity arises for input at the acquisition stage, the spouses should be advised to consider acquiring individually owned annuities rather than a single annuity of which only one spouse is the owner, particularly when marital property funds are used for the acquisition. In that case, the separate annuities should be classified in a marital property agreement as the individual property of the respective spouses.

From an estate tax planning standpoint, annuities are not a favored source for funding a credit shelter trust since they will constitute income in respect of a decedent (at least in part). Hence, like a deferred employment benefit or IRA, discussed at sections 10.132– 10.160, *infra*, the annuity should be one of the assets of last resort for funding a credit shelter trust.

### **G. Stock Options [§ 10.99]**

The manner in which stock options are classified under marital property law is discussed in chapter 2, *supra*. As with life insurance or annuities, creating certainty regarding the classification of stock options is important from a planning standpoint if the option holder's spouse is not designated to receive the holder's interest in stock options upon the death of the holder. Further, it is important to consider whether the terminable interest rule should or should not apply to stock options classified as marital property when the nonholding spouse dies first. For a discussion of the terminable interest rule, see section 10.139, *infra*.

There is some uncertainty regarding whether stock options constitute "deferred employment benefits" within the meaning of subsections 766.01(3m) and (4). See *supra* ch. 2. If the spouses are entering into a marital property agreement, the agreement can specify whether stock options are to be regarded as deferred employment benefits. Generally, such treatment is advisable since the terminable interest rule will avoid a testamentary disposition of the nonholding spouse's marital property interest if he or she predeceases the holding spouse. In some instances,

however, the nonholding spouse may have insufficient assets with which to fund a credit shelter trust should he or she die first. In that situation, providing specifically in a marital property agreement that the stock options are classified as marital property and that the terminable interest rule does not apply to the stock options may aid in funding the credit shelter trust if the nonholding spouse dies first.

In planning for stock options, the applicable instrument creating the stock option interest should be examined. In some instances, an interest in stock options passes by beneficiary designation. In others, the deceased holder's rights with respect to stock options may be exercised only by his or her personal representative. In the latter case, administration proceedings will be required to effectively exercise the stock option rights (and hence passing the stock options by will substitute agreement may be ill-advised).

## **H. Closely Held Business Interests [§ 10.100]**

### **1. Sole Proprietorships [§ 10.101]**

The item-by-item rule, under which the classification of assets is determined on an individual basis (rather than aggregate), *see supra* ch. 2 and § 10.10, may make classification an important issue in planning for spouses when one of them conducts business as a sole proprietor. Unless the estate plan of each spouse provides for all assets of the business to pass to the survivor, the assets making up the business may become owned as tenants in common by the survivor and a third party.

➤ **Example.** A wife operates a successful home-based business as a sole proprietor. She intends to leave the business to her daughter from a prior marriage upon her death and so provides in her will. The wife predeceases her husband. A number of the business assets are classified in whole or in part as marital property. As a result, the husband becomes a tenant in common with the wife's estate and eventually the wife's daughter with respect to a number of the business assets. Alternatively, if the husband were to predecease the wife and leave his estate to a third party, the husband's estate and eventually the third party would become a tenant in common with the wife as to those business assets classified as marital property.

To avoid these results, the spouses can reclassify (by marital property agreement or other means) the business assets as the wife's individual property, thereby giving only the wife the power to make a testamentary disposition of the business assets. A further step that might be taken to simplify the identification of the business assets would be for the wife to conduct her business as a single-member LLC, with her LLC interest then classified as her individual property. A single-member LLC is taxed in the same manner as a sole proprietorship, *see* Treas. Reg. § 301.7701-3, and there is the added benefit of limited liability that comes with operating as a limited liability entity.

Note that the classification problem in the above example is not necessarily solved by simply having the husband make a provision in his will leaving all of his marital property interest in the wife's business to her. Although this would eliminate the identified problem if the husband were to die first, the problem would remain if the wife died first, because the husband would continue to own a one-half interest in each marital property asset.

In the above example, if the spouses were unable to agree on classifying the wife's business assets as her individual property, she could still ensure that the business would pass to her daughter and not be subject to testamentary disposition by the husband by incorporating the business and then utilizing a directive as contemplated by section 857.015. *See* Wis. Stat. §§ 857.015, 766.70(3). For a discussion of section 857.015, *see* chapter 4, *supra*. (Of course, any business assets held by both spouses in the "and" form would require the husband's joining in a conveyance to the corporation.) Note that a directive authorized under section 857.015 is available in the case of a closely held corporation but not in the case of assets of an unincorporated business or an interest in an LLC (other than arguably a professional LLC, *see* Wis. Stat. § 766.70(3)(b)).

*See* section 10.10, *supra*, describing the option of deviating from the item-by-item rule by virtue of the change made to section 766.31(3) by 2005 Wisconsin Act 216, section 42.

## **2. Corporations [§ 10.102]**

When one or both spouses' property includes an interest in a closely held corporation, a number of planning issues may be presented. Those

applicable will depend on the spouses' particular goals and objectives. The following is a summary of some of the major issues that may apply.

Ascertaining the classification of the stock of the corporation is important for a thorough consideration of the planning alternatives. The task may be as simple as examining an existing marital property agreement or the form in which title is held (for example, if issued after 1986 while the spouses were domiciled in Wisconsin, title held in the names of husband and wife as "marital property," "survivorship marital property," "tenants in common," or "joint tenants" will determine the classification; *see* Wis. Stat. § 766.60). In other instances, ascertaining the classification may be a more difficult task, requiring consideration of the time, manner, or source of acquisition of the stock the extent of postdetermination date appreciation in the value of the stock and the extent to which a spouse working in the business received compensation during that period, the extent to which earnings have been retained in the corporation, and other factors. *See supra* ch. 2. Ultimately, to achieve certainty regarding the classification of corporate stock, it may be advisable for the spouses to enter into a marital property agreement that, among other things, classifies the stock either as marital property or individual property.

Deciding how to classify closely held stock in a marital property agreement requires consideration of a number of factors, which may include one or more of the following: (1) the effect of reclassification on the spouses' relative property rights during the marriage, in the event of dissolution, or upon the death of one spouse; (2) the potential impact of reclassification with respect to potential creditor claims; (3) the need to balance the spouses' respective estates for effective marital deduction/credit shelter planning; (4) the opportunity to obtain a full adjustment in the basis of the stock upon the death of either spouse if it is classified as marital property; (5) the extent to which classification as marital property would facilitate estate or gift tax valuation discounts with respect to transfers of the stock; and (6) other factors not listed.

In addition, to the extent there are multiple shareholders, the planner should examine any buy-sell arrangements already in place or the advisability of adopting a buy-sell arrangement to create certainty regarding succession of ownership. With respect to an existing arrangement, the planner should ascertain the extent to which it contemplates disposition of the stock not only upon the death of the stockholder spouse but also upon the death of the nonholding spouse if

the stock is classified as marital property. See chapter 4, *supra*, for a discussion of buy-sell agreements and alternatives for addressing the disposition of the nonholding spouse's marital property interest if he or she dies first.

When the planner is representing only one spouse, the representation may include advice designed to maximize that spouse's management and control rights and power of disposition over stock of the corporation.

### 3. S Corporations [§ 10.103]

Planning issues for S corporations under I.R.C. §§ 1361–1379 are similar to those for C corporations, with some additional considerations relating to making and maintaining the S corporation election. As discussed in chapter 9, *supra*, each person having a community property interest in the stock or income of a corporation must consent to an S corporation election. In view of the income rule under section 766.31(4), which generally classifies the income from nonmarital property as marital property, both spouses should consent to the election even if the stock is the nonmarital property of one spouse.

If an effective S corporation election has been made and the stock is classified as marital property, consideration should be given to the effect the death of one spouse could have with respect to the continued validity of the election.

➤ **Example.** S corporation stock classified as marital property is given to an irrevocable trust designed to effect a completed gift for transfer tax purposes but to be “defective” for income tax purposes. The grantor trust rules under I.R.C. §§ 671–678 cause the income to be taxed to the husband and wife, and the trust (a grantor trust) is an eligible shareholder pursuant to I.R.C. § 1361(c)(2). The wife subsequently dies.

Upon the wife's death, as to one-half of the trust, the trust is no longer a grantor trust. While the trust would continue to qualify as an S corporation shareholder for two years, *see* I.R.C. § 1361(c)(2)(A)(ii), action will be required at some point to preserve the S corporation election (for example, the trustee's electing to treat the trust as an electing small business trust under I.R.C. § 1361(e)). For a further

discussion of marital property considerations regarding intentionally defective grantor trusts, see section 10.124, *infra*.

#### **4. Partnerships [§ 10.104]**

Marital property issues in planning, with respect to a closely held partnership, are essentially the same as those in planning with respect to a closely held corporation. Note, however, that it may be necessary for the partnership to make certain elections to obtain the full basis adjustment for marital property assets held by the partnership. *See supra* ch. 9.

#### **5. LLCs [§ 10.105]**

Marital property issues in planning with respect to a multiple member LLC are essentially the same as those in planning with respect to a partnership when the LLC has elected under the “check-the-box” regulations to be taxed as a partnership. *See* Treas. Reg. § 301.7701-3. Note, however, that a directive authorized under section 857.015 is available in the case of a closely held corporation but not in the case of assets of an unincorporated business or an interest in a LLC (other than, arguably, a professional LLC, *see* Wis. Stat. § 766.70(3)(b)). *See* chapter 4, *supra*, for a discussion of the directive under section 857.015, sometimes referred to as a “statutory” buy-sell provision.

An LLC owned solely by a husband and wife as community property under the laws of a state can be regarded either as a disregarded entity or a partnership, at the taxpayer’s option. Rev. Proc. 2002–69, 2002–44 I.R.B. 831, 2002–2 C.B. 831.

#### **6. Professional Partnerships [§ 10.106]**

The marital property issues in planning with respect to a professional partnership or other entity will depend, in part, on the manner in which it is organized (i.e., as a corporation, partnership, LLC, etc.). The above discussions relating to corporations, partnerships, or LLCs should be consulted depending on the form of organization. Specific provisions under Wisconsin law prohibit a person not licensed in a particular profession from holding an interest in a professional entity. *See, e.g.,*

Wis. Stat. § 180.1911 (providing that each shareholder, director, and officer of a service corporation must be licensed, certified, or registered by a state agency in the same field of endeavor). It is particularly important in the case of such entities, therefore, that an appropriate buy-sell arrangement be in place that contemplates the disposition of an ownership interest not only upon the death of the professional but also upon the death of the professional's spouse when the ownership interest is marital property. See chapter 4, *supra*, and section 10.128, *infra*, for discussion of buy-sell agreements and alternatives for addressing the disposition of the nonholding spouse's marital property interest if he or she dies first.

### **I. Deferred Employment Benefits and IRAs [§ 10.107]**

The marital property issues involved in planning with respect to deferred employment benefits and IRAs are of considerable complexity and therefore are addressed separately at sections 10.132–.147 and 10.148–160, respectively, *infra*.

### **J. Assets Acquired by Gift or Transfer at Death [§ 10.108]**

Assets acquired by a spouse as a gift or transfer at death are classified as individual property. Wis. Stat. § 766.31(7)(a). In a joint representation the planner should consider whether that classification should be changed. Reasons for changing the classification from individual property to marital property include balancing the spouses' estates for estate tax planning reasons and making the assets eligible for a full basis adjustment upon the death of either spouse. However, before reclassifying assets received by a spouse by gift or transfer at death, the estate planner should carefully consider the potential adverse effects on the spouse who received the gift or transfer at death.

First, by reclassifying such assets as marital property, the owning spouse gives up valuable property rights, including the right to make a testamentary disposition of 100% of the assets. Even if the owning spouse retains management and control of the assets, he or she is bound by a duty of good faith toward the other spouse with respect to such assets, and any transfer of the assets may be subject to the remedies

under section 766.70. For a discussion of these remedies generally, see chapter 8, *supra*.

Second, if the assets are reclassified as marital property, their availability to satisfy obligations incurred by either spouse is expanded. *See* Wis. Stat. § 766.55(2). For a discussion of creditors' rights with respect to marital property assets, see chapter 6, *supra*, and sections 10.171–.177, *infra*.

Third, assets received by gift or transfer at death that are reclassified as marital property may be part of the divisible estate in the event of dissolution, whereas otherwise they would have been nondivisible (except in the case of hardship) under section 767.255. 2005 Wisconsin Act 443 renumbered the property division statute from section 767.255 to section 767.61.

### **K. Non-Wisconsin Real Estate [§ 10.109]**

Spouses who are domiciled in Wisconsin (and thus are governed by chapter 766) may own real estate in another jurisdiction (for example, a second residence). The extent to which such non-Wisconsin real estate may be affected by the classification rules of Wisconsin's marital property law is not always clear because of the vagaries of conflict-of-laws analysis. For a general analysis of conflict of laws as relating to community property law, see chapter 13, *infra*.

Because traditional conflict-of-laws analysis generally favors a legal characterization in accordance with the law of the situs, *see infra* ch. 13, the manner in which spouses acquire title to real property in another jurisdiction may create questions regarding its classification, notwithstanding the use of marital or community property funds to acquire the property. *See, e.g.,* Rev. Rul. 68-80, 1968-1 C.B. 348 (Virginia property acquired by spouses as tenants in common using proceeds from sale of New Mexico community property did not qualify for full adjustment in basis under I.R.C. § 1014(b)(6)); *see supra* ch. 9. For example, if Wisconsin-domiciled spouses purchase real property in Florida using marital property funds and take title to that property as tenants by the entireties, their ownership rights in the property may be governed by Florida law, not Wisconsin's marital property law. While some states have given a level of recognition to community property rights by adopting the Uniform Disposition of Community Property



Rights at Death Act, promulgated by the National Conference of Commissioners on Uniform State Laws in 1971 [hereinafter Uniform Disposition Act], such recognition may be incomplete. *See, e.g.*, Fla. Stat. § 732.218 (Uniform Disposition Act as adopted in Florida not applicable to property owned by spouses as tenants by the entireties). For a discussion of the Uniform Disposition Act, see chapter 13, *infra*.

On the other hand, if marital property funds have been used to acquire non-Wisconsin real estate and the title has been taken in the name of one spouse alone, the property should be classified as marital property. See chapter 13, *infra*, for a discussion of possible procedural solutions for the difficulties that might be faced in convincing the court in another state to recognize Wisconsin marital property interests in real estate located there.

Because spouses will often want their interests in real property located in another jurisdiction to be treated as community property for purposes of the full adjustment of basis rule under I.R.C. § 1014(b)(6), it is useful to consider ways to accomplish that result that will prevent the uncertainties associated with a potentially conflicting form of title in the situs state. One way is to convert the spouses' interest in real property to an interest in intangible personal property by, for example, contributing the non-Wisconsin real estate to a partnership or LLC of which the spouses are the owners. A partnership interest or an LLC membership interest is personal property, not real property. *See* Wis. Stat. §§ 178.22, 183.0703. Generally the law of the spouses' domicile (in this case Wisconsin) governs ownership rights in intangible personal property. *See infra* ch. 13. Hence, by converting the real property interest to an interest in personal property, the spouses should be able to specify application of Wisconsin law and classify their partnership or LLC interests as marital property. For a discussion of tax basis adjustment rules applicable to partnership interests (or LLC interests) and the underlying partnership (or LLC) property, see chapter 9, *supra*.

If spouses are acquiring non-Wisconsin real estate using marital property funds, another way to preserve community property treatment for federal tax purposes is to acquire the non-Wisconsin real property in a revocable living trust designed to hold marital property assets of the spouses. Title to the non-Wisconsin real property will be held by the trustees (likely the spouses) and the terms of the trust instrument can provide for continued recognition of the spouses' respective ownership rights with respect to marital property assets held by the trust. For a

discussion of the IRS's position with respect to community property held in a revocable living trust, see chapter 9, *supra*.

Another question is whether Wisconsin-domiciled spouses may reclassify non-Wisconsin real estate as marital property when the property was not acquired with marital property assets.

➤ **Example.** A husband inherits his parents' condominium, located in a common law property jurisdiction that has adopted the Uniform Disposition Act. The husband and his wife, who are domiciled in Wisconsin, later enter into a marital property agreement classifying all their assets, however titled and wherever situated, as marital property.

Would the condominium thereafter be classified as marital property? Under the facts in the example, the Uniform Disposition Act would not apply to the property, since it only applies to "real property situated in this [the situs] state which was acquired with the rents, issues or income of, the proceeds from, or in exchange for, property acquired as, or which became, and remained, community property under the laws of another jurisdiction, or property traceable to that community property." Uniform Disposition Act, § 1(2), 8A U.L.A. 121 (1983). On the other hand, under conflict-of-laws analysis, Wisconsin law might govern the classification since Wisconsin arguably would have a greater interest in the property rights of the spouses. *See* Introductory Note to Topic 2, Chapter 9 of the Restatement (Second) Conflict of Laws, reproduced in part in chapter 13, *infra*. Wisconsin's marital property law does not purport to place a jurisdictional limitation on the situs of property that may be classified as marital property. Hence, a strong argument can be made that Wisconsin law should apply and govern the classification of the non-Wisconsin real estate. From a planning standpoint, without the Uniform Disposition Act to provide support in recognizing the marital property status of the reclassified asset, the spouses could facilitate the future recognition of their respective marital property rights by transferring title of the property to a revocable trust that includes provisions requiring the trustees to treat the property in the same manner as other marital property assets.

## **L. Intellectual Property Rights [§ 10.110]**

Spouses' property interests may include intellectual property rights (e.g., patents, copyrights, or trademarks). Wisconsin's marital property law provides no special classification rules for intellectual property rights, but the general classification rules under section 766.31 should provide a sufficient basis for allowing intellectual property interests to be classified as marital property. However, as discussed in this section, there are significant issues relating to federal preemption, particularly in the case of copyrights and patents.

Subject to the federal preemption concerns noted below, a general opt-in marital property agreement that classifies spouses' assets as marital property could reclassify intellectual property rights as marital property, or it may merely confirm that classification if the property interests at issue were accrued during the marriage. In some instances, however, the spouse who holds the property interest (for example, a copyright to a book that he or she wrote) may want to maintain complete ownership and control of the asset under all circumstances, including the death of the other spouse. In that case, reclassification of the copyright as marital property could undermine the objective of the holding spouse.

From an estate tax planning standpoint, the classification of an intellectual property right as a marital property asset may facilitate the use of both spouses' applicable credit amount. See sections 10.84–.86, *supra*, for a discussion of unified credit/marital deduction planning.

From an income tax planning standpoint, the question arises whether the full basis adjustment rule for community property under I.R.C. § 1014(b)(6) is applicable to intellectual property rights classified as marital property. I.R.C. § 1221(a)(3) provides in part that a “copyright, literary, musical or artistic composition, a letter or memorandum, or similar property” is not a capital asset if held by a taxpayer who personally created the property. If the asset is not a capital asset, it cannot receive a basis adjustment. On the other hand, if a patent or copyright is treated as a capital asset in the hands of a decedent (i.e., if it was purchased by the decedent), there is no reason the basis adjustment rule would not apply.

Whether state community property laws are preempted by the federal copyright law has been the subject of litigation, with conflicting results. In *Worth v. Worth*, 241 Cal. Rptr. 135 (Ct. App. 1987), the California

Court of Appeals concluded that federal law did not preempt California's community property law with respect to the ownership of a copyright. In *Rodrigue v. Rodrigue*, 55 F. Supp. 534 (E.D. La. 1999), *aff'd* 218 F.3d 432 (5th Cir. 2000), the U.S. District Court for the Eastern District of Louisiana specifically rejected the analysis in *Worth* and held that the federal copyright law preempts Louisiana community property law on the question of ownership of copyrights. The district court in *Rodrigue* did not consider, however, whether spouses could voluntarily classify a copyright as community property. On appeal, the Fifth Circuit Court of Appeals reversed, concluding that although the author-spouse retains exclusive management and control of a copyright, the economic benefits of the copyright belong to the community. *Rodrigue*, 218 F.3d at 435.

Unlike retirement plan assets governed by ERISA, copyrights are assignable, and the copyright law specifically recognizes joint ownership of copyrights. See 17 U.S.C. § 201. Hence, while the litigation in *Rodrigue* and *Worth* creates some uncertainty regarding the effect of community property laws on copyright ownership, the federal law would appear to accommodate planning by spouses who wish to voluntarily adopt community property as the form of ownership of a copyright. Patents, which share the same constitutional foundation as copyrights, see U.S. Const. Art. I, § 8, cl. 8, and which likewise are subject to assignment and joint ownership, see 35 U.S.C. §§ 261 and 262, arguably should be treated in the same manner.

For a general discussion of estate planning for intellectual property rights, see David H. Melnick et al., "Intellectual Property Issues in Estate Planning," Practising Law Institute, 29th Annual Estate Planning Institute, 267 PLI/Est 371 (1998).

### **M. Planning Trust Interests for Beneficiaries [§ 10.111]**

Parents often are concerned with the marital property implications for property received from them by their children, either as a lifetime gift or a transfer at death. Assuming the application of Wisconsin law to the child, property received by gift or transfer at death is classified under chapter 766 as individual property. Wis. Stat. § 766.31(7)(a). Similarly, for purposes of property division in the event of dissolution, property received by gift or transfer at death from a third party is nondivisible, absent hardship. Wis. Stat. § 767.61. Hence, if the child takes the necessary steps to segregate the donated or inherited property, its

classification under chapter 766 and its character under chapter 767 can be preserved. But income from the property will be classified as marital property under chapter 766 (absent an effective marital property agreement or unilateral statement providing otherwise) and will be divisible upon dissolution under chapter 767 (absent an effective marital property agreement providing otherwise).

Parents making lifetime gifts or transfers at death to children can provide a greater level of protection under both chapter 766 and 767 by creating trust interests for their children. Under section 766.31(7)(a), both the principal and income of a trust created by a third party are classified as the individual property of the donee. Similarly, under chapter 767, the court of appeals held in *Friebel v. Friebel*, 181 Wis. 2d 285, 510 N.W.2d 767 (Ct. App. 1993), that income accumulated in and distributed from a discretionary trust created by a third party was not divisible upon dissolution. Deciding whether to use a trust for this purpose involves balancing a number of considerations, including the loss of flexibility on the part of the child beneficiary and the income and transfer tax implications of creating a long-term trust interest.

Other means of insulating assets and enhancing the ability to identify them as having their source in a gift or transfer at death is to make the subject of the gift or transfer at death an interest in a partnership, LLC, or other interest.

It should be observed, of course, that not all spouses who are governed by Wisconsin's marital property laws have married children governed by the same laws: married children may reside in other jurisdictions that have other laws respecting marital property rights in gifts or inheritances, whether made outright, in trust, or in the form of an entity interest. A discussion of the laws of various jurisdictions that could apply to the donees or legatees of married Wisconsin spouses is beyond the scope of this book.

## **XII. Specific Estate Planning Techniques and Situations**

### **[§ 10.112]**

#### **A. Annual Exclusion Gifts [§ 10.113]**

Gifts qualifying for the gift tax annual exclusion under I.R.C. § 2503(b) may be made with marital property assets or nonmarital property assets by the spouse (or spouses) having management and control. *See* Wis. Stat. § 766.51(4). If marital property assets are the subject of the gift and one spouse acts alone, the other spouse may have a remedy under section 766.53, although for wealthier spouses a gift exceeding the \$1,000 statutory amount in section 766.53 but within the annual exclusion amount under I.R.C. § 2503(b) may be considered “reasonable in amount considering the economic position of the spouses.” Wis. Stat. § 766.53. For a discussion of remedies relating to gifts of marital property assets, see chapter 8, *supra*.

A spouse making a gift of his or her nonmarital property assets over which he or she has management and control need not be concerned with lifetime remedies by the other spouse. However, if the donor spouse dies within two years of making the gift and the subject of the gift was deferred marital property under section 851.055, the augmented deferred marital property estate includes the value of the property. Wis. Stat. § 861.03(4).

If one spouse acting alone gives assets to a third-party donee, it is important to know the classification of the assets to identify the donor or donors for federal gift tax purposes. If the assets given are nonmarital property, the spouse making the gift is the only donor for federal gift tax purposes. If the assets given are marital property, both spouses are deemed donors for federal gift tax purposes even though only one spouse acted in making the gift. *See supra* ch. 9. Thus, for example, one spouse may make a gift of marital property assets having a value of \$22,000 to a third party donee and, provided no other gifts are made to the same donee during the calendar year by either spouse, the gift would be within the annual exclusion amount for each spouse, thereby making the filing of a gift-splitting election on IRS Form 709 unnecessary. Note, however, that if the subject of the gift is a difficult-to-value asset (such as closely held stock), it may nonetheless be advisable to file gift tax returns in order to commence the running of the gift tax statute of limitation. *See* I.R.C. §§ 6075, 6501; Treas. Reg. § 301.6501(c)-1.

## **B. Taxable Gifts [§ 10.114]**

Gifts that exceed the amount of the federal gift tax annual exclusion or that do not qualify for the annual exclusion because of failure to meet the “present interest” requirement under I.R.C. § 2503(b) are referred to in this section as *taxable gifts*. Taxable gifts may or may not result in the payment of federal gift tax depending on whether or not the donor has fully used the \$1 million federal gift tax exemption under I.R.C. § 2505.

Taxable gifts may be made with marital property assets or nonmarital property assets by the spouse (or spouses) having management and control. *See* Wis. Stat. § 766.51(4). If marital property assets are the subject of the gift and one spouse acts alone, the other spouse may have a remedy under section 766.53, although the gift is a completed transfer by reason of section 766.51(4). *See supra* ch. 9. For a discussion of remedies relating to gifts of marital property assets, see chapter 8, *supra*.

If a donor spouse makes a gift of nonmarital property assets that are deferred marital property under section 851.055 and dies within two years of making the gift, the augmented deferred marital property estate includes the value of the assets given. Wis. Stat. § 861.03(4).

If one spouse acting alone gives assets to a third-party donee, it is important to know the classification of the assets to identify the donor or donors for federal gift tax purposes. If the assets given are nonmarital property, the spouse making the gift is the only donor for federal gift tax purposes. If the assets given are marital property, both spouses are deemed donors for federal gift tax purposes even though only one spouse acted in making the gift. *See supra* ch. 9. Thus, for example, if one spouse makes a gift of marital property assets having a value of \$200,000 to a third-party donee, each spouse is deemed to have made a gift of \$100,000 to the donee. Each spouse must file a federal gift tax return since each is a donor and the gift exceeds the amount of the gift tax annual exclusion under I.R.C. § 2503(b). If the amount of the gift exceeds the amount of a spouse’s gift tax exemption under I.R.C. § 2505, that spouse owes federal gift tax.

## **C. Generation-skipping Transfers [§ 10.115]**

For transfers during lifetime, a donor for federal gift tax purposes is treated as the transferor for purposes of the federal GST tax. *See* I.R.C.

§ 2652(a)(1)(B). Hence, when marital property assets are the subject of a gift, for GST tax purposes each spouse is deemed to be the transferor of one-half of the transferred assets. *See supra* ch. 9. Thus, for purposes of determining qualification for the GST tax annual exclusion under I.R.C. § 2642(c), the allocation of the GST exemption under I.R.C. §§ 2631 and 2632, or liability for GST tax under I.R.C. § 2603, consideration must be given to the classification of the property transferred. If the subject of a transfer is nonmarital property and spouses make a gift-splitting election pursuant to I.R.C. § 2513, for GST tax purposes each spouse is treated as a transferor with respect to one-half of the gift. I.R.C. § 2652(a)(2).

For transfers taking effect at death, the decedent is treated as the transferor for GST tax purposes for any property subject to the estate tax. *See* I.R.C. § 2652(a)(1)(A). Thus, for example, the decedent is the transferor for GST tax purposes of his or her one-half interest in former marital property assets passing at death, since such assets are includible in the decedent's estate under I.R.C. § 2033. It is important, therefore, in the case of residuary dispositions that involve generation skipping (either direct skips or transfers in trust that could ultimately result in a taxable termination) to understand the full extent of the property interests over which the decedent has a power of disposition—including his or her one-half marital property interest in assets titled in the name of his or her spouse. The use of formula provisions based on the available GST exemption often are used to ensure that transfers make optimal use of the GST exemption but do not result in the imposition of GST tax.

#### **D. Disclaimers [§ 10.116]**

The use of a disclaimer following the death of a decedent can be a useful postmortem estate planning technique. The requirements of Wisconsin law must be considered for the disclaimer to be effective for property law purposes, and the requirements of federal law must be considered for the transaction to be nontaxable for gift tax purposes. Further, at the pre-death planning stage, consideration must be given to the classification of assets to maximize flexibility for the possible later use of a disclaimer.

Section 854.13 governs disclaimers with respect to all types of transfers of property. For a general discussion of the statute, see Howard S. Erlanger, *Wisconsin's New Probate Code* § 4.03 at 133 (1998). Section 854.13 is drafted broadly to authorize disclaimer with respect to



virtually any kind of gratuitous transfer of property, including by a “beneficiary under a governing instrument.” Wis. Stat. § 854.13(1)(a), (2). The term *governing instrument* is defined broadly under section 854.01 to include a myriad of instruments that can effect a transfer of property, both during life and at death, including a will substitute provision under section 766.58(3)(f). For a discussion of transfers by will substitute provisions in a marital property agreement, see chapter 7 and sections 10.64–.69, *supra*. Section 854.13 also includes a specific provision authorizing a surviving spouse to disclaim a deceased spouse’s interest in survivorship marital property, Wis. Stat. § 854.13(2)(c), as well as a specific provision authorizing a surviving joint tenant to disclaim a survivorship interest in joint tenancy property, Wis. Stat. § 854.13(2)(b). In addition, while the statute does not specifically refer to disclaimers with respect to joint accounts under chapter 705, the term *governing instrument* under section 854.01 includes “an instrument under ch. 705,” and although the term *instrument* is not defined in chapter 705, the reference in section 854.01 has been interpreted to include joint or P.O.D. bank accounts. See Erlanger, *supra*, § 4.01 at 86.

For a disclaimer to be qualified and therefore not treated as a gift for federal gift tax purposes, it must comply with the requirements of I.R.C. § 2518 and the regulations thereunder. There are five basic requirements for a disclaimer to be qualified under I.R.C. § 2518: (1) it must be irrevocable and unqualified; (2) it must be in writing; (3) the writing must be delivered in a timely manner (generally within nine months of the event creating the property interest); (4) the disclaimant must not have accepted the interest disclaimed or any of its benefits; and (5) the interest disclaimed must pass either to the spouse of the decedent or a person other than the disclaimant without any direction on the part of the disclaimant. Treas. Reg. § 25.2518-2(a).

Final regulations adopted in 1997 regarding the disclaimer of joint interests have settled any concerns that may have existed with respect to the time in which a qualified disclaimer of a decedent’s interest in survivorship marital property must be made. Although the final regulations do not mention survivorship marital property (or its analogue, community property with right of survivorship), they do settle, in a manner favorable to taxpayers, the timing issue with respect to disclaiming the survivorship interest in jointly owned property that is not unilaterally severable. Like tenancy by the entirety property, marital property (including survivorship marital property) is not unilaterally severable. See *supra* ch. 2. Treas. Reg. § 25.2518-2(c)(4)(i) provides:

“A qualified disclaimer of a survivorship interest to which the survivor succeeds by operation of law upon the death of the first joint tenant to die must be made no later than 9 months after the death of the first joint tenant to die regardless of whether such interest can be unilaterally severed under local law....” Example 8 of Treas. Reg. § 25.2518-2(c)(5) extends the application of the quoted section to tenancy-by-the-entirety property. The same rationale should apply to a disclaimer by a surviving spouse of the deceased spouse’s interest in survivorship marital property.

The regulations also address the timing and extent to which a surviving spouse or other co-owner of a joint bank, brokerage, or other investment account may make a qualified disclaimer of a deceased joint owner’s interest. Under the regulations, if a surviving joint owner wishes to disclaim contributions to an account made by a deceased co-owner, the disclaimer must be made within nine months of the deceased co-owner’s death, and the surviving co-owner may not disclaim any portion of the joint account attributable to considerations furnished by the surviving co-owner. Treas. Reg. § 25.2518-2(c)(4)(iii). Of course, if the property in the account were classified as marital property, then the disclaimer would be limited to one-half of the value of the account at the death of the deceased co-owner.

The regulations under I.R.C. § 2518 do not contemplate the timing or extent to which a disclaimer may be made with respect to property passing under a will substitute agreement as authorized by section 766.58(3)(f) or by the laws of the state of Washington. However, in Private Letter Ruling 95-07-017 (Feb. 17, 1995), the IRS considered a disclaimer with respect to property passing to the surviving spouse under a Washington community property agreement and concluded that “for purposes of section 2518(a)(2), the 9-month period for making the disclaimer of the decedent’s one-half community property interest passing to [surviving spouse] under the community property agreement commences on the date of death.”

When an estate plan contemplates that property will pass to the surviving spouse but that the surviving spouse might disclaim the property so that it can pass to another person or entity (e.g., a child or a credit shelter trust), consideration should be given to the classification of the property at issue. If an asset is classified as marital property, the surviving spouse already owns an undivided one-half interest in the property; hence, he or she cannot disclaim more than the decedent’s one-half interest in the property. *See* Treas. Reg. § 25.2518-2(c)(5), example

11. The following illustrates the application of the regulation in the case of Wisconsin spouses:

➤ **Example.** A husband is the owner and insured of a \$700,000 face-amount life insurance policy acquired after the spouses' determination date. Under section 766.61(3)(a), the policy is classified as marital property. The husband designates his wife as primary beneficiary and a credit shelter trust of which the wife is a beneficiary as the contingent beneficiary of any death proceeds. Upon the husband's death, the wife may make a qualified disclaimer of no more than one-half of the death proceeds since she already has a one-half ownership interest in the proceeds.

Note that in this example, the insurer will likely be unaware of any classification issues and will simply follow its ownership records in administering the policy and its proceeds. See Wis. Stat. § 766.61(2)(b). If the wife were to submit a complete (as opposed to a partial) disclaimer, the insurer would pay the proceeds to the designated contingent beneficiary. If the wife thereafter failed to recover her one-half interest in the proceeds, adverse transfer tax consequences could result. *Whiteley v. United States*, 214 F. Supp 489 (W.D. Wash. 1963). Careful drafting of the disclaimer to make it clear that the disclaimer relates only to the decedent's one-half marital property interest in the proceeds (and not to the interest of the surviving spouse) will avoid such adverse transfer tax consequences.

## **E. Irrevocable Life Insurance Trusts [§ 10.117]**

The acquisition of life insurance by an irrevocable trust established by the insured is a popular technique for transferring wealth without estate tax. Careful drafting is required to avoid having the insured possess any incidents of ownership in the policy that could cause estate tax inclusion under I.R.C. § 2042.

If the insured's spouse is a life beneficiary of the irrevocable life insurance trust, particular attention must be given to the classification of the assets used to fund the trust. As noted in section 9.92, *supra*, for federal tax purposes, the husband and wife are treated as equal grantors when community property assets are transferred. Thus, if the husband gives marital property assets to an irrevocable trust and the wife is a beneficiary of the trust, she will be treated as having made a transfer of

one-half of the assets given by the husband. If the wife has a beneficial interest in the trust, upon her death, the portion of the trust attributable to her one-half interest in the assets transferred to the trust is vulnerable to inclusion under I.R.C. § 2036 as a transfer with a retained interest. *See supra* ch. 9.

The best solution to this problem is to have the donor-insured use only individual property funds for the initial and periodic gifts to the trust. If such individual property assets exist, they should be maintained as a segregated fund with measures taken to ensure that they retain their classification as individual property (such as the owner's executing and delivering a unilateral statement under section 766.59 or the spouses' entering into a marital property agreement under section 766.58).

In many instances, however, there will be no existing pool of individual property assets to serve as the source of periodic gifts by the insured to the irrevocable life insurance trust. In that case, the spouses could agree in a marital property agreement that certain assets that otherwise would be classified as marital property will be classified as individual property, or the reclassification could be accomplished by a gift from one spouse to the other. The reclassified assets could then be used as the source of the gifts by the insured to the trust. Or, the spouses could agree in a marital property agreement that any assets transferred to the trust are classified as the individual property of the insured. Although there is no direct authority on point, these techniques should be effective to avoid a transfer with a retained interest. However, some commentators have expressed the need for caution in this area. *See, e.g., Price, supra* § 10.1, at § 6.23.6. Notwithstanding the risk, the survivor's estate will still be better off from an estate tax standpoint, because the portion of the trust attributable to the donor-insured's one-half interest will not be subject to inclusion in the gross estate of the surviving spouse.

The question may arise regarding the extent to which a written consent under section 766.61(3)(e) may be a useful means of avoiding the complications of marital property classification in the context of an irrevocable life insurance trust. Section 766.61(3)(e) provides that a written consent in which a spouse consents to the use of property to pay premiums on a policy is effective, "to the extent that the written consent provides, to relinquish or reclassify all or a portion of that spouse's interest in property used to pay premiums on the policy or in the ownership interest or proceeds of the policy without regard to the

classification of property used by a spouse or another person to pay premiums on that policy.” It is arguable that a contribution to an irrevocable life insurance trust is not property used to pay a premium at the time of the gift to the trust (since the trustee is not obliged to invest the contributed funds in life insurance premiums). Subject to the issues noted above, a marital property agreement is a more flexible and comprehensive way to accomplish the reclassification.

If the insured’s spouse is not a beneficiary of the irrevocable life insurance trust (for example, if the trust is solely for the benefit of the insured’s descendants), there is no concern that part of the trust will be a transfer with a retained interest under I.R.C. § 2036, even if marital property assets are used as the source of periodic gifts to the trust. Other concerns can exist, however. For example, if the donor-insured directly pays the premiums on a policy owned by the irrevocable life insurance trust with marital property funds, consideration must be given to the effect of section 766.61(3)(d) if the insured’s spouse survives the insured. That section provides that, in the case of a policy that designates a person other than either spouse as the owner, if no premium on the policy is paid from marital property after the determination date, chapter 766 does not affect the ownership interest and proceeds of the policy. The section goes on to provide, however, that if a premium on the policy is paid from marital property funds after the determination date, the ownership interest and proceeds of the policy are in part the property of the designated owner of the policy and in part marital property of the spouses, regardless of the classification of property used to pay premiums on that policy after the initial payment of a premium on it from marital property funds. Read literally, this means in the context of an irrevocable life insurance trust that the surviving spouse has a right to claim a portion of the proceeds of the policy. Moreover, the failure of the surviving spouse to assert his or her claim within the time period specified by section 766.70(6) could result in the surviving spouse being treated as having made a taxable gift to the trust. *See supra* ch. 9.

The application of section 766.61(3)(d) will most likely be avoided if the donor-insured does not pay the premiums on the policy directly but instead makes periodic gifts to the trustee of the irrevocable life insurance trust, who in turn pays the premiums on the policy. Even if the periodic gifts to the trust are made with marital property funds, once given to the trust the funds are no longer marital property, and hence the trustee does not pay premiums with marital property funds. In that instance, however, there is still the possibility that the spouse could have

a remedy under section 766.70 with respect to the gift of marital property assets, if the amount given exceeds the limits under section 766.53. *See supra* ch. 8. These concerns are eliminated, of course, if the funds used by the donor-insured to make gifts to the trust are classified as individual property. For a more detailed discussion of section 766.61(3)(d), *see* chapter 2.

So-called second-to-die life insurance, which pays a death benefit upon the death of the second to die of two insureds, has become a popular means of creating a source of liquidity at the death of the surviving spouse. Such insurance is often acquired by the trustee of an irrevocable life insurance trust with funds contributed to the trust by the insureds. Since both spouses are insureds, neither is a beneficiary of the trust and thus there should be no problem with the spouses' contributing marital property assets to the trust. For the reasons discussed previously relating to section 766.61(3)(d), it is advisable that insurance premiums not be paid with marital property funds directly by the donors but instead by the trustee with funds given to the trust by the donors.

## **F. Valuation Discount Planning [§ 10.118]**

### **1. In General [§ 10.119]**

The marital property system offers opportunities for valuation discount planning in a variety of contexts. Appraisers and the IRS recognize that the valuation of closely held stock and partnership interests often must be discounted because of a general lack of marketability or when the interest being valued constitutes only a minority interest. Further discounts may be available for built-in capital gains or when a key person is necessary to the business. When real estate is involved, discounts will reflect the limitations of holding fractional undivided interests.

A discount for lack of marketability is given when it is difficult to reduce an asset to cash. More time is needed for the sale of stock in a closely held company, and transactional costs generally are higher than those applicable in a sale of an interest in a publicly traded company. A lack-of-marketability discount can be given even when a controlling interest in a company is involved.

In the context of a business entity such as a corporation or partnership, a discount of a minority interest takes account of the interest holder's lack of control and lack of a right to participate in management decisions, compensation decisions, decisions involving distributions of income, such as declarations of dividends, and the ultimate disposition of business assets through sale, merger, or liquidation.

Discounts for minority interests and fractional interests in an asset are inherent in a community property system. If an asset is entirely marital property, the most a spouse can own is 50%. At the death of a spouse, assets can be retitled to reflect the former marital property interests, and during the lifetimes of the spouses marital property interests can be reclassified as individual property interests to take advantage of certain estate planning opportunities.

The subject of valuation and discounts is discussed at chapter 9, *supra*. Also, see Price, *supra* § 10.1, at §§ 2.44 and 11.1.2, regarding valuation discounts generally.

## **2. Discounts at Death of First Spouse [§ 10.120]**

The leading case is *Estate of Bright v. United States*, 658 F.2d 999 (5th Cir. 1981). Mr. and Mrs. Bright lived in a community property state. Together they owned 55% of the outstanding stock in two closely held companies and their affiliates. At Mrs. Bright's death, her husband was appointed executor of her estate. The IRS attempted to value Mrs. Bright's interest as part of one 55% interest through a "family attribution" argument. The court rejected that argument, treated her 27.5% interest as the only asset to be valued, and granted a discount for a minority interest.

Subsequently, in Rev. Rul. 93-12, 1993-1 C.B. 202, the IRS conceded that the reasoning in *Bright* is correct, and that the family attribution argument is incorrect. In the situation underlying the ruling, the donor, who owned all the stock of a closely held company, gave each of his five children a 20% interest. Despite total loss of control by the donor, each gift was valued separately with discounts for lack of marketability and minority interest.

Using a marital property agreement that classifies closely held stock or partnership interests as marital property, Wisconsin spouses can put

themselves into precisely the position of the Brights. The interests of the deceased spouse and surviving spouse will not be aggregated for valuation purposes. The interest of the deceased spouse, therefore, can be discounted for lack of control.

The size of a block of stock can influence valuation. If all outstanding stock in a closely held company is marital property, the first spouse to die holds a 50% interest. A 50% interest is more than a minority interest but less than full control and is entitled to some discount. There is a potentially deeper discount if the deceased spouse's interest is less than 50%. It may be desirable, therefore, to give some shares to children (or other desired beneficiaries) during the lifetimes of the spouses.

What of the swing-vote argument adopted by the IRS in Technical Advice Memorandum 9436005 (Sept. 9, 1994)? In that ruling, the IRS took the position that a 30% block of stock could not be discounted significantly because it could combine with another 30% block to control the company. The IRS had raised that issue in *Bright*, but the court rejected the issue because the IRS had not raised it in the district court and “no miscarriage of justice [would] result.” In *Furman v. Commissioner*, 75 T.C.M. (CCH) 2206 (1998), the Tax Court rejected the IRS's swing-vote argument in a case in which a husband and wife each gave a 6% interest in a closely held business to their son, who already owned a 40% interest. The Tax Court nonetheless allowed a combined minority interest/lack of marketability discount of 40% for each 6% block. See also *Estate of Davis v. Commissioner*, 110 T.C. 530 (1998) (rejecting swing-vote theory).

### **3. Death of Second Spouse [§ 10.121]**

Another significant case involving a community property state is *Estate of Bonner v. United States*, 84 F.3d 196 (5th Cir. 1996). In this case, real estate was held as community property when Mrs. Bonner predeceased her husband. At Mrs. Bonner's death, Mr. Bonner took ownership of his half of the community property real estate. Mrs. Bonner's estate plan provided for her half to pass to a QTIP marital trust. When Mr. Bonner later died, the IRS attempted to aggregate the interests in his estate and in the QTIP marital trust for valuation purposes, noting that both were included in his estate for federal estate tax purposes albeit under separate sections of the I.R.C., section 2033 for his ownership



interest and section 2044 for the interest in the QTIP marital trust. The court rejected the IRS's position and held that the case was controlled by the reasoning of *Estate of Bright*, 658 F.2d 999 (5th Cir. 1981). The court held that the QTIP interest had to be valued separately, because neither of the I.R.C. sections cited by the IRS required or logically contemplated that the QTIP assets would merge with other assets. Further, Mr. Bonner had no control over their ultimate disposition. Thus, the QTIP assets could pass as Mrs. Bonner directed. The court would not consider evidence regarding who actually received the assets.

In *Estate of Mellinger v. Commissioner*, 112 T.C. 4 (1999), the Tax Court followed the Fifth Circuit's reasoning in *Bonner*, concluding that two blocks of approximately 28% each in the publicly traded stock of Frederick's of Hollywood, Inc. should not be aggregated for valuation purposes when one block was includible in the surviving spouse's estate under I.R.C. § 2033 and the other was includible under § 2044. *See also Estate of Nowell v. Commissioner*, T.C.M. (RIA) 99, 015; *Estate of Lopes v. Commissioner*, 78 T.C.M. (CCH) 46 (1999).

Thus, marital property can be arranged so as to obtain discounts at the deaths of both spouses—in the first estate because of the inherent minority or fractional aspect of the asset being valued, and in the second by having placed the one-half interest of the first spouse to die in a QTIP marital trust. Caution dictates that a surviving spouse not be given a general power of appointment over the marital property interest owned by the first spouse to die and that there may be some risk in a special power as well. Naming the surviving spouse as sole trustee of the QTIP marital trust should not create a problem because of the fiduciary duties of a trustee and the trustee's lack of power of ultimate disposition at the surviving spouse's death.

#### **4. Fractional Interests [§ 10.122]**

Fractional interests in the same asset are discounted for valuation purposes below the price the asset itself would bring if sold in its entirety to a willing buyer. Issues involving this discount often arise in connection with real estate. Usually the issue is the method of calculating the discount. The IRS has taken the position that the discount should be limited to the cost of partition. *See, e.g.*, Tech. Adv. Mem. 9336002 (Sept. 10, 1993). The courts, however, have allowed discounts based on the time it takes to partition, the lesser value that may be

obtained because the partitioned parcel is smaller in size, the inability to borrow using an undivided interest as collateral, and the fact that it may be necessary to deal with the other owner in operating the real estate. In *Estate of Williams v. Commissioner*, 75 T.C.M. (CCH) 1758 (1998), the Tax Court allowed an unprecedented discount of 44% for gifts of undivided interests in Florida timberland. See also *LeFrak v. Commissioner*, 66 T.C.M. (CCH) 1297 (1993) (in valuing undivided interests in real property, Tax Court allowed combined discount of 30% for fractional interest and lack of marketability).

Questions regarding the extent of the discount aside, there are clear implications for marital property. Fractional interest discounts will likely be available in connection with any parcel of marital property real estate because the ownership is inherently fractionalized between the spouses. At the death of a spouse, the asset is divided between the deceased spouse's estate and the surviving spouse. See *Propstra v. United States*, 680 F.2d 1248 (9th Cir. 1992) (allowing 15% fractional interest discount when interest transferred was decedent's one-half community property interest).

During the spouses' lifetimes, management and control will depend on how the real estate is titled. If the parcel is titled in the name of only one spouse, that spouse can manage and control the asset, and the other spouse has no authority of disposition over the interest he or she owns (note, however, in the case of homestead real property, both spouses must join in any conveyance, regardless of how title is held, see Wis. Stat. § 706.02(1)(f)). Note, however, that a valid waiver of homestead rights in a marital property agreement eliminates the need for the nontitled spouse's signature. See *Jones v. Estate of Jones*, 2002 WI 61, 253 Wis. 2d 158, 646 N.W.2d 280. The nature of management and control poses no difficulty in connection with gifts of interests to third parties in which both spouses participate. The gift of an interest should be discounted under normal principles.

## **G. Personal Residence Trusts [§ 10.123]**

A personal residence trust under I.R.C. § 2702 can be a powerful planning technique to transfer value to the next generation at reduced transfer tax cost. For a general discussion of personal residence trusts, see Price, *supra* § 10.1, at §§ 9.44–.44.4.

Under the governing regulations, a personal residence is defined as either the principal residence of the trust term holder under I.R.C. § 1034 or one other residence that would be treated as the term holder's dwelling under I.R.C. § 280A(d)(1) (without regard to § 280A(d)(2)) or an undivided fractional interest in either). Treas. Reg. § 25.2702-5(b)(2). A trust of which the term holder is a grantor is not a personal residence trust if at the time of the transfer, the term holder already holds a term interest in two trusts that are personal residence trusts of which the term holder was the grantor. Treas. Reg. § 25.2702-5(a). Hence, a husband and wife together could participate in up to three personal residence trusts, one for their principal residence (whether owned by the husband, the wife, or both), one that is the wife's separate property, and one that is the husband's separate property.

➤ **Note.** I.R.C. § 1034 was repealed by Public Law 105-34, 111 Stat. 788 (1997), although Treas. Reg. § 25.2702-5 has not been amended to reflect that repeal.

Given the above rules, consideration should be given to the classification of property transferred to a personal residence trust. If a personal residence is owned as marital property and the spouses wish to establish a personal residence trust arrangement for that residence, there are three alternatives.

First, the spouses together may create a joint personal residence trust and transfer the property to the trust. The governing regulations provide that spouses may transfer their interests in a residence to the same personal residence trust if the trust instrument prohibits anyone other than a spouse from holding a term interest in the residence concurrently with the other spouse. Treas. Reg. § 25.2702-5(b)(2)(iv). While this alternative would not require the spouses to reclassify the property before transferring it to the trust, given the complexity of drafting a joint personal residence trust, this is not the most straightforward alternative.

Second, the spouses may first reclassify the property as the individual property of one spouse, and then the owner spouse may transfer the property to a personal residence trust of which that spouse is the term holder (the other spouse must join in the conveyance if the property is homestead property). If the spouses intend to create personal residence trusts with both a principal residence and a second residence, this is the most straightforward arrangement, with each spouse creating a personal

residence trust with his or her own individual property. This method also preserves the spouses' ability to create a third personal residence trust.

Third, the spouses may wish to create separate personal residence trusts, to which each transfers a fractional interest in the same residence. This approach reduces the risk that the arrangement will completely fail to achieve the desired tax objective (because of the term holder's death before the end of the trust term). Since marital property is not unilaterally severable, *see supra* ch. 2, a residence owned as marital property by the spouses should be reclassified as tenancy-in-common property before conveyance to the spouses' respective personal residence trusts—otherwise, each spouse could arguably be treated as a grantor of each trust. *See* Priv. Ltr. Rul. 99-31-028 (tenancy-by-the-entirety property reclassified as tenancy-in-common property before spouses' conveyance to their respective personal residence trusts). *But see* Priv. Ltr. Rul. 199908032 (Feb. 26, 1999) (approving separate personal residence trusts (one for each spouse) when spouses conveyed one-half interests in community property residence to respective trusts). The fractional interest passing into each personal residence trust should be entitled to a fractional interest discount.

Regardless of how a personal residence is classified or titled, if it is the homestead of the spouses, both spouses must join in the conveyance of the property to the personal residence trust for the transfer to be effective. *See* Wis. Stat. § 706.02(1)(f). *But see* Priv. Ltr. Rul. 199908032 (Feb. 26, 1999) (approving separate personal residence trusts (one for each spouse) when spouses conveyed one-half interests in community property residence to respective trusts).

## **H. Intentionally Defective Grantor Trusts [§ 10.124]**

The grantor trust rules under I.R.C. §§ 671 and 678 require that, under certain circumstances, the grantor of a trust (or a beneficiary, in the case of I.R.C. § 678) be treated as the owner of all or a portion of a trust for income tax purposes as long as the grantor is living. As a result of differences between the income and transfer tax provisions of the I.R.C., it is possible to create an irrevocable trust that constitutes a completed transfer for gift and estate tax purposes but that will nonetheless result in the grantor being taxed on the income under the grantor trust rules. The use of such a trust can provide tax benefits from an estate planning standpoint by allowing the assets of an irrevocable trust to accumulate on

an effectively income tax-free basis, since the income tax is paid by the grantor. Such trusts often are referred to as *intentionally defective grantor trusts*. For a general discussion of this planning technique, see Price, *supra* § 10.1, at §§ 10.32–.32.8. For a discussion of grantor trust issues raised by the transfer of marital property, see chapter 9, *supra*.

When community property assets are transferred, the husband and wife are treated as equal grantors for federal tax purposes. Thus, if a husband gives marital property assets to an irrevocable trust for the benefit of his descendants, both he and his wife are treated as the grantors of the trust for federal tax purposes. If the trust is a grantor trust under I.R.C. §§ 671 or 678 and one spouse dies, as to that spouse, the grantor trust rules would cease to apply and the trust thereafter would have a dual character for income tax purposes—one-half of the income would be taxed to the surviving spouse, and the other one-half would be taxed to the trust. This result may lead to unnecessary complications in income tax reporting or, worse, could result in the unanticipated termination of S corporation status if S corporation stock is held by the trust and Subpart E status (treating grantors as substantial owners) was the basis for treating the trust as an eligible shareholder. See I.R.C. § 1361(c)(2)(A)(i).

To avoid such complications or unanticipated results, nonmarital property assets are a better subject of a gift to an intentionally defective grantor trust. If necessary, an asset can be reclassified as an individual property asset before its contribution to the trust. For a discussion of the various means of reclassifying assets, see chapter 2, *supra*.

## **I. Grantor Retained Annuity Trusts (GRATs) [§ 10.125]**

In the right circumstances a grantor retained annuity trust (GRAT) can produce significant estate tax benefits. A GRAT is much like the qualified personal residence trust described in section 10.123, *supra*, except that assets other than a personal residence are used (for example, closely held stock), and the grantor retains an annuity of a set dollar amount from the trust for its term. The retained annuity interest is valued based on IRS tables and subtracted from the value of the property placed in the trust on the date of transfer, with only the difference subject to gift tax. If the grantor dies during the term of the trust, the value of the trust assets at the date of death is included in the grantor's estate for federal estate tax purposes, but if he or she survives the term, the trust assets and

all appreciation pass to the beneficiaries without further tax. GRATs are specifically sanctioned by I.R.C. § 2702 as an exception to special valuation rules providing that, for most gifts with a retained interest, the retained interest of the donor is to be valued at zero (thereby increasing the amount of the gift for gift tax purposes).

Neither I.R.C. § 2702 nor the corresponding regulations provide authority for a joint transfer of property by spouses to a GRAT. For that reason alone, it is advisable to avoid transferring marital property assets to a GRAT. Moreover, it is important that a GRAT be treated as a grantor trust for income tax purposes pursuant to the grantor trust rules under I.R.C. §§ 671–678. Grantor trust treatment is important if a portion of the property transferred to the GRAT (for example, shares of stock) must be transferred back to the grantor in satisfaction of the annuity payment. Generally, satisfaction of a pecuniary obligation by transferring appreciated property causes recognition of gain; however, if the transaction is between an individual and a trust of which the individual is treated as the owner for income tax purposes, no gain is recognized. When marital property assets are transferred to a GRAT, each spouse is deemed to have transferred one-half of the assets to the trust. If the trust is treated as a grantor trust for income tax purposes and one spouse dies, one-half of the trust ceases to have grantor trust status. *See supra* ch. 9. Other complications can arise as well relating to the inclusion of one-half of the value of the trust in the deceased spouse's estate for estate tax purposes under I.R.C. § 2036.

These concerns can be addressed by reclassifying the marital property interests as the spouses' individual property so that each can create a GRAT, or reclassifying all interests as the individual property of one spouse so that he or she can create the GRAT. The choice will depend on the circumstances, such as the relative ages of the spouses. For a discussion of the various means of reclassifying assets, see chapter 2, *supra*.

In T.D. 9181, 2005-1 C.B. 717, the Treasury announced final regulations conforming the gift tax regulations defining a qualified interest for purposes of I.R.C. § 2702 to the Tax Court's decision in *Walton v. Commissioner*, 115 T.C. 589 (2000), *acq. in result*, I.R.S. Notice 2003-72, 2003-2 C.B. 964. *See* Qualified Interests, 70 Fed. Reg. 9222 (Feb. 25, 2005). In *Walton*, the court declared example 5 of Treas. Reg. § 25.2702-3(e) to be invalid in regard to the valuation of an interest includible in a donor's estate with respect to a failed GRAT (a failed

GRAT is one as to which the grantor did not survive past the specified term of the GRAT).

## **J. Charitable Remainder Trusts [§ 10.126]**

A trust that qualifies as a charitable remainder trust under either I.R.C. § 664(d)(1) (as a charitable remainder annuity trust) or under I.R.C. § 664(d)(2) (as a charitable remainder unitrust) can provide a tax-advantageous way for a donor or donors (provided they are husband and wife) to make lifetime or testamentary gifts that benefit one or more individuals and charities. For a general discussion of charitable remainder trusts, see Price, *supra* § 10.1, at §§ 8.20 to 8.29.

When an inter vivos charitable remainder trust is established by a married donor, it is important to consider the classification of the assets contributed to the trust. Generally, marital property complications can be avoided if individual property is contributed to the trust. If the subject of the gift to the trust is a marital property asset, the spouses can reclassify the asset as individual property before the transfer to the trust.

It is possible, however, to establish a charitable remainder trust using marital property assets. When marital property assets are contributed to a charitable remainder trust, the better approach is to have both spouses designated as grantors of the trust. Having both spouses act as grantors eliminates any questions regarding whether the spouses have joined in the gift or the availability of a remedy by the nondonor spouse. For a discussion of gifts and remedies generally, see chapter 8, *infra*.

Moreover, when both spouses are designated as grantors of the charitable remainder trust, each can reserve under the trust instrument the power, exercisable by will, to revoke the survivor's interest with respect to one-half of the trust. See Treas. Reg. § 1.664-2(a)(4). While the reservation of such power is unnecessary to avoid gift tax upon establishment of the trust (because of the availability of the gift tax marital deduction, as set forth in Treas. Reg. § 25.2523(g)-1), if the spouses were to subsequently divorce, the reserved power could be exercised by each spouse so that, upon the death of the first spouse, one-half of the value of the trust would pass to the charitable remainder beneficiary and qualify for the estate tax charitable deduction in the deceased spouse's estate. For a sample form of a charitable remainder

trust established jointly by spouses with community property, see 2 Conrad Teitell, *Deferred Giving* (1971) 10-35, ¶ 10.01[A].

## K. Charitable Lead Trusts [§ 10.127]

Charitable deductions are allowed for income, gift, and estate tax purposes for a gift to charity of a current interest in a trust that pays a guaranteed annuity or unitrust interest for a fixed term or for the life or lives of persons in being at the creation of the interest. I.R.C. §§ 170(f)(2)(B), 2522(c)(2)(B), 2055(e)(2)(B). For a general discussion of charitable lead trusts, see Price, *supra* § 10.1, at § 8.31.

A charitable contribution for income tax purposes is allowed only when the donor will be taxed on the income of the trust under the grantor trust rules. I.R.C. § 170(f)(2)(B). This would occur if the trust reverts to the grantor after the charitable term. When the remainder is not retained by the grantor but rather is vested in other noncharitable beneficiaries, the value of the charity's annuity or unitrust interest is not deductible for income tax purposes, and accumulated income (including capital gains) is taxed to the trust.

If the noncharitable remainder is not retained by the grantor, there should be no problem with giving marital property assets to a charitable lead trust. The net gift for gift tax purposes (i.e., the difference between the value of the property given and the present value of the charitable annuity or unitrust interest), is deemed to have been transferred one-half by each spouse. See *supra* ch. 9.

If the noncharitable remainder is retained by the grantor, such that the trust is taxed as a grantor trust, transferring marital property assets to the charitable lead trust could lead to unnecessary complications. When the trust is a grantor trust under I.R.C. §§ 671–678 and one spouse dies, the grantor trust rules cease to apply to that spouse and the trust thereafter has a dual character for income tax purposes—one-half of the income is taxed to the surviving spouse, and the other one-half is taxed to the trust.

These complications can be avoided by reclassifying the marital property interests as the spouses' individual property so that each can create a charitable lead trust, or reclassifying all interests as the individual property of one spouse so that he or she can create a charitable



lead trust. The choice will depend on the circumstances, such as the relative ages of the spouses.

## **L. Buy-sell Agreements [§ 10.128]**

If the spouses' property includes a closely held business interest (whether in the form of stock, partnership interest, or LLC interest), the estate planner should review any buy-sell agreement affecting the interest. If the interest is the nonmarital property of one spouse, no particular marital property issues are implicated. However, if the interest is classified as marital property, the agreement should be examined with respect to its effect at the deaths of both the holding spouse and the nonholding spouse, since each spouse owns an undivided one-half interest in the item.

If the holding spouse dies first, the terms of a buy-sell agreement, to the extent applicable, will be operative with respect to the entire business interest held by that spouse (i.e., both the deceased holding spouse's one-half interest and the surviving nonholding spouse's one-half interest). *See Wis. Stat. § 766.51(10).*

If the nonholding spouse dies first, the disposition of the deceased spouse's one-half interest will be controlled by the agreement to the extent the agreement so provides. *Wis. Stat. § 766.51(10).* However, some buy-sell agreements do not include provisions that address the disposition of the nonholding spouse's interest if he or she dies before the holding spouse. They may also fail to address such circumstances as the insolvency of the nonholding spouse or dissolution of the marriage. If the agreement does not address these situations, and the objective is to have the titled spouse maintain management and control regardless of a change in circumstances, several courses of action should be considered.

The most comprehensive approach is for the buy-sell agreement to be amended by the principals (e.g., the shareholders if a corporation) to include provisions such as those described in section 4.82, *supra*, so that, for example, if the nonholding spouse predeceases the holding spouse, the holding spouse will have the first option to acquire the deceased nonholding spouse's shares, with successive options in the other shareholders or corporation. This course of action has the advantage of "fixing" the problem not only for the spouses who are the planner's clients, but also for the other shareholders, which may be important to

maintaining control of the entity within an identified class of individuals or their family members. It also has the advantage of addressing not only the nonholding spouse's dying first but also circumstances of insolvency or divorce.

In some instances, the planner or his or her clients may not be in a position to effect a change in the buy-sell agreement. As between the spouses, at least in the context of the nonholding spouse's dying first, the transfer to the surviving holding spouse of the deceased spouse's one-half marital property interest can be ensured by including a provision in a will substitute agreement that provides for the nonholding spouse's interest to pass to the holding spouse without probate. See chapter 7, *supra*, and sections 10.64–69, *supra*, for a discussion of will substitute agreements. A less certain approach (because of the revocable nature of wills) is to include in the nonholding spouse's will a specific bequest of the interest to the holding spouse.

The disposition of the nonholding spouse's interest directly to the survivor, however, may be inconsistent with the spouses' estate tax planning—that is, the value of the predeceasing nonholding spouse's interest may be needed to fund a credit shelter trust. Or, in some instances, the nonholding spouse may choose not to leave his or her interest to the holding spouse. In either situation, the surviving holding spouse can use a directive under section 857.015 to require that the nonholding spouse's marital property interest in the closely held business interest be satisfied from other property. Note, however, that the types of entities to which a directive under section 857.015 applies are those listed in section 766.70(3)(a), (b), and (d), which do not include an LLC (although arguably a professional association organized as an LLC would be included within subsection (3)(b) as a “similar entity”).

For a more detailed discussion of buy-sell agreements, see chapter 4, *supra*.

## **M. Planning for the Incapacitated Spouse [§ 10.129]**

Mentally disabled spouses may be in need of estate planning. In some states, a guardian for an incompetent person may take some estate planning actions for the incompetent person under the “doctrine of substituted judgment.” However, this doctrine is not always applied by the Wisconsin courts. See *Michael S.B. v. Berns (In re Guardianship of*

*Stanley B.*), 196 Wis. 2d 920, 540 N.W.2d 11 (Ct. App. 1995); *Kellogg-Citizens Nat'l Bank of Green Bay v. Borden (In re Guardianship of Hougard)*, 107 Wis. 2d 599, 321 N.W.2d 313 (Ct. App. 1982).

Some estate planning may be possible under such a power of attorney if the power is executed before the person becomes incompetent. For example, an agent under a durable power of attorney may make gifts on behalf of the principal if the power of attorney document grants such authority. No reported decision in Wisconsin has considered whether an agent under a durable power of attorney may enter into or amend a marital property agreement on behalf of an incapacitated spouse, even when that authority is specifically granted in the durable power of attorney document.

Under section 766.51(7), a court may appoint a guardian or conservator under chapter 54 to exercise a disabled spouse's right to manage and control marital property. *Management and control* is defined broadly in section 766.01(11). Moreover, section 766.51(4) provides that the right to manage and control marital property includes the power to make gifts, subject to the remedies under chapter 766 (*see* Wis. Stat. § 766.53). In that regard, section 54.20(2)(h) may assist some estate planning actions, not only with regard to marital property assets but also with regard to nonmarital property assets. That section provides that a guardian of the estate, may exercise, with the court's approval, any management and control right over property, whether or not marital property, that the married person could exercise under chapter 766 if the person were not under guardianship. Section 54.20(2)(h) also provides that the guardian may act together or join in any transaction for which consent or joinder of both spouses is required, or may execute a marital property agreement with the other spouse. Section 54.20(2)(h) expressly provides, however, that the guardian may not make, amend, or revoke a will.

In *V.D.H. v. Circuit Court (In re Guardianship of F.E.H.)*, 154 Wis. 2d 576, 453 N.W.2d 882 (1990), the Wisconsin Supreme Court set forth standards for the application of section 880.173 (the predecessor to section 54.20). In that case, the co-guardians for the incompetent husband petitioned the court to permit the transfer of the husband's interest in the homestead (owned in joint tenancy with the spouse) to his spouse and daughter. The circuit court denied the petition, saying that the transfer might require that the husband be supported by the Wisconsin taxpayers. If that happened, the circuit court stated, it would

be approving something contrary to public policy. The court of appeals affirmed. The supreme court reversed. It noted that section 880.173 codified the common law doctrine of substituted judgment and stated:

[T]he Wisconsin legislature intended to authorize the guardian of the estate of a married ward to exercise, with the approval of the court, any property right which the ward could exercise on his or her own behalf if he or she were of full capacity, except the power to make, amend, or revoke a will. We therefore hold that the legal standard which the circuit court is to apply in deciding whether to approve the exercise of power by the guardian of the estate under sec. 880.173 is whether the exercise of power will benefit the ward, his or her estate, or members of his or her immediate family....

Moreover, the circuit court's determination that public policy precludes the proposed transfer is erroneous. In fact, public policy as expressed in the statutes and regulations dealing with the administration of the medical assistance program specifically endorses this type of transfer, regardless of its possible adverse effect on the availability of assets to pay for the care of an institutionalized ward.

*Id.* at 589–90.

For a number of examples of actions that can be taken by a guardian with the approval of the court, see Nontax Provisions of the Marital Property Implementation Law: Original and Supplemental Explanatory Notes (1985 Wisconsin Act 37), Wisconsin Legislative Council Staff Information Memorandum 85-7, Part I, at 118–19 [hereinafter 1985 Trailer Bill Original Nontax Note to § xxx.xx or 1985 Trailer Bill Supplemental Nontax Note to § xxx.xx, as appropriate]. The uncaptioned original and supplemental notes can also be found in Wisconsin Statutes Annotated following the pertinent statutory section.

## **N. Planning for Spouses Moving from Wisconsin**

### **[§ 10.130]**

Wisconsin's marital property law applies only when both spouses are domiciled in Wisconsin. *See* Wis. Stat. §§ 766.01(8), .03(2). If one or both spouses moves from Wisconsin, the marital property law ceases to apply, although property rights acquired and obligations incurred while the law applied continue. Wis. Stat. § 766.03(3). There may be significant advantages to spouses in preserving the classification of marital property assets after a move from Wisconsin, including the

preservation of equalized estates for estate tax planning purposes and the preservation of the potential for a full adjustment in basis upon the death of one spouse.

The fact that assets were at one time held as marital or community property does not ensure that they will receive favorable treatment for basis adjustment purposes at death, as indicated in Rev. Rul. 68-80, 1968-1 C.B. 348. Under the facts of the ruling, the husband and wife owned real property in New Mexico as community property. In 1965 they moved to Virginia and traded their community property in New Mexico for real property in Virginia, to which they took title as tenants in common. The husband died in 1966 and by will left his undivided one-half interest in the Virginia property to the wife. The wife then sold the property. The question in the ruling was whether the wife was entitled to claim a step-up in basis to the value at the husband's death for her one-half interest in the property pursuant to I.R.C. § 1014(b)(6). The IRS ruled that the wife's basis in her undivided one-half interest was her cost, stating: "There is nothing in the Internal Revenue Code or regulations that would indicate that section 1014(b)(6) of the Code relating to 'community property held' was intended to include separate property that had previously been converted from community property to separate property."

Revenue Ruling 68-80 should not discourage attempts to preserve the classification of marital property assets when there is a change of domicile to a common law property state. The problem for the taxpayer in the ruling was the state property law conclusion reached by the IRS, which dictated the federal tax result—the spouses failed to preserve the asset's community property character. Community property character for federal tax purposes has been recognized in the case of a change of domicile to a common law property state. *See, e.g., Johnson v. Commissioner*, 88 F.2d 952 (8th Cir. 1937) (following move from community property state, ordinary income and capital gain from community property assets continued to be recognized as owned equally by spouses for purposes of filing separate income tax returns).

The keys to preserving the classification of marital property assets after either spouse is no longer domiciled in Wisconsin are (1) adequately segregating marital property assets from nonmarital property assets acquired either before or after terminating the Wisconsin domicile; and (2) avoiding titling of marital property assets in a manner that, under local law, destroys the incidents of marital property or

disqualifies the property from application of the Uniform Disposition Act.

After establishing the new domicile, spouses should avoid taking title to marital property assets in a co-tenancy form of ownership such as tenancy in common, joint tenancy with right of survivorship, or tenancy by the entirety. Avoidance of the tenancy-in-common form of ownership is warranted by reason of Rev. Rul. 68-80, *see supra* § 10.109, although the Uniform Disposition Act was not in effect in Virginia at the time of the ruling, and hence the application of the ruling under similar facts when the new state of domicile has adopted the Uniform Disposition Act is uncertain. However, as for co-tenancy forms of ownership that include a right of survivorship, the Uniform Disposition Act offers little support, as it provides that title taken in a form that includes a right of survivorship is presumed to be property to which the uniform act does not apply. Uniform Disposition Act, § 2(2), 8A U.L.A. 121 (1983). Of course, if the new jurisdiction of domicile is another community property jurisdiction, local law may provide that property held in the name of both spouses is community property. When the new state is a common law property jurisdiction, unless a revocable trust is used to segregate and identify marital property assets, marital property assets should be held in the name of one spouse or the other, not jointly, and should not be commingled with newly acquired assets.

A joint funded revocable trust is an excellent vehicle for segregating and identifying marital property assets, particularly if it has been drafted in contemplation of holding marital property assets. A sample form for a joint revocable living trust can be found in section 10.177, *infra*. Note, however, that the provisions of the form relating to the classification of income from nonmarital property assets held by the trust will need to be modified upon a change of domicile, since after Wisconsin's marital property law no longer applies, income from nonmarital property in a common law jurisdiction will most likely be classified under local law as some form of separate property.

It is uncertain whether income from marital property will continue to be regarded as marital property after spouses terminate their Wisconsin domicile. When either spouse is no longer domiciled in Wisconsin, section 766.31(4), which classifies income from property as marital property, no longer applies. *See* Wis. Stat. § 766.03(3). Under general choice-of-laws rules, local law—that is, the law of the new domicile—will govern the classification of income from personal property and real

estate in the new domicile. Where applicable, the Uniform Disposition Act treats the “rents, issues and income of” community property in the same manner as the underlying property. Uniform Disposition Act, § 1, 8A U.L.A. 121 (1983). This is essentially a recognition under local law that the income of an asset has the same characteristics as the asset itself. In addition, if the spouses while domiciled in Wisconsin entered into an opt-in marital property agreement classifying income from marital property as marital property regardless of a change of domicile, further support is available under the Restatement (Second) of Conflict of Laws. Restatement § 258, Comment d, states: “The rule of this Section [that the law of the spouses’ domicile at time of acquisition controls] is not applicable if a valid contract between the spouses provides otherwise.” Hence, an argument can be made, particularly in states that have adopted the Uniform Disposition Act or in the case of spouses who have a marital property agreement with supporting provisions, that even after terminating a Wisconsin domicile, the income from marital property assets is classified as marital property. The most cautious approach, however, is to segregate post-Wisconsin-domicile income from the underlying marital property assets to avoid an argument that there has been a commingling of marital and nonmarital property assets.

If spouses planning a move from Wisconsin have entered into a marital property agreement (such as an opt-in agreement), the agreement should be reviewed to make sure it adequately expresses an intent to have the classification provisions continue to apply in the case of marital property acquired while both spouses were domiciled in Wisconsin. Further, if the marital property agreement contains a will substitute provision under section 766.58(3)(f), consideration should be given to eliminating the provision because of questions regarding the extent to which such provisions will be given effect in another jurisdiction and the extent to which such provisions may be amended following termination of a Wisconsin domicile. *See infra* ch. 13.

## **O. Planning for Noncitizen Spouses [§ 10.131]**

Absent careful planning, adverse transfer tax consequences can result when property interests are transferred between spouses and the transferee spouse is not a U.S. citizen. A community property regime in which the reclassification of property interests is possible (for example, Wisconsin’s marital property law) presents a trap for the unwary.

The application of Wisconsin's marital property law to spouses does not take into account the spouses' citizenship. While both spouses must be domiciled in Wisconsin for the law to apply, *see supra* ch. 2, neither is required to be a U.S. citizen. However, if one or both of the Wisconsin domiciled spouses is not a U.S. citizen (but rather is a resident alien), specific estate and gift tax provisions must be considered in the estate planning process. *See supra* ch. 9.

The I.R.C. generally taxes resident aliens the same as U.S. citizens with respect to estate, gift, and generation-skipping transfer taxes. However, in the case of both the estate tax and the gift tax, there are limitations on the availability of the marital deduction, and in the case of the estate tax, there is a special rule regarding the inclusion of joint tenancy or tenancy by the entireties property in the deceased spouse's gross estate.

For gift tax purposes, the marital deduction is allowable (subject to general limitations in the case of terminable interests) if the donee spouse is a U.S. citizen, regardless of the citizenship or residency of the donor spouse. If the donee spouse is not a U.S. citizen, the marital deduction is denied. However, the gift tax annual exclusion under I.R.C. § 2503(b) is increased to \$100,000 for gifts to a spouse so long as the gift is of a present interest and otherwise would qualify for the gift tax marital deduction. I.R.C. § 2523(i).

With regard to the estate tax, if the surviving spouse is a U.S. citizen, the marital deduction is available to the deceased spouse's estate irrespective of the deceased spouse's citizenship or residency. However, if the surviving spouse is not a U.S. citizen, the marital deduction is not available regardless of the deceased spouse's citizenship and residency, with two exceptions. *See* I.R.C. § 2056(d)(1). First, the marital deduction is available if the surviving spouse was a U.S. resident continuously after the decedent's death and became a U.S. citizen before the estate tax return was due (including extensions). I.R.C. § 2056(d)(4). Second, the marital deduction is available if the property passes to a "qualified domestic trust" meeting the requirements of I.R.C. § 2056A(a) and regulations thereunder. I.R.C. § 2056(d)(2)(A).

Another consequence of the surviving spouse's not being a U.S. citizen relates to the includability of property owned by spouses as joint tenants or as tenants by the entireties. The general rule under I.R.C. § 2040(b) is that only one-half of property owned between a husband and



wife as joint tenants with right of survivorship or as tenants by the entirety is includible in the deceased spouse's gross estate. This general rule is altered by I.R.C. § 2056(d)(1)(B), which provides that, if the surviving spouse is not a U.S. citizen, I.R.C. § 2040(a) governs instead—that is, the gross estate includes the entire value of such property to the extent that the surviving spouse did not provide consideration.

There are potential adverse tax consequences of reclassifying assets when either spouse is a noncitizen, and thus extreme caution should be used in reclassifying property as part of the estate planning process. As discussed in section 9.109, *supra*, the reclassification of an asset *from* individual property of one spouse *to* marital property is deemed a gift of one-half of the value of the asset for federal gift tax purposes. Likewise, reclassifying an asset *from* marital property *to* individual property of one spouse is deemed a gift. If on an annual basis the amount of the deemed gift to the noncitizen spouse is less than \$100,000, no gift tax is payable as long as the subject of the gift is a present interest and not a terminable interest. But if the amount of the deemed gift exceeds \$100,000 in any year, gift tax may be payable or the donor's applicable credit amount may be partially or completely used, or both.

Moreover, when one spouse is a noncitizen, caution should be used regarding the manner in which title to assets is acquired. Taking title in a particular form (e.g., as joint tenants or as survivorship marital property) can effect a reclassification, *see supra* ch. 2. For example, when both spouses are domiciled in Wisconsin, if nonmarital property funds of one spouse are used to acquire assets for which title is taken by the spouses as tenants in common or joint tenants, the nonmarital property becomes marital property or survivorship marital property. *See* Wis. Stat. § 766.60(4)(b). Moreover, certain forms of title (e.g., survivorship marital property, joint tenancy or joint account ownership) include a right of survivorship that causes property to pass outright to the surviving spouse. For citizen and noncitizen spouses alike, this result can undermine marital deduction/credit shelter planning; for a surviving noncitizen spouse, it includes the added complication of not qualifying for the marital deduction (although the property passing to the surviving noncitizen spouse will be treated as having passed to a qualified domestic trust if the property is transferred or irrevocably assigned to a qualified domestic trust before the decedent's estate tax return is filed. I.R.C. § 2056(d)(2)(B)).

On the other hand, a community property system provides more opportunity to shift wealth to a noncitizen spouse: if property is acquired while both spouses are domiciled in Wisconsin, it is classified as marital property absent the ability to identify a reason why it should be classified as individual property (e.g., by showing that it was inherited). Hence, if the noncitizen spouse survives, he or she claims one-half of each marital property asset without concern for the marital deduction limitations under the I.R.C. The surviving noncitizen spouse may subsequently be able to remove his or her half of former marital property assets from the U.S. transfer tax system—something a U.S. citizen spouse could not do.

➤ **Practice Tip.** If spouses decide not to enter into a marital property agreement because of the concerns about interspousal transfers noted in this section, it may be useful for them to sign a memorandum verifying the source of acquisition of their assets, particularly when assets may have been acquired while the spouses were domiciled in a community property jurisdiction (for example, France). The memorandum could provide valuable evidence of classification later for a spouse's personal representative or the surviving spouse.

### **XIII. Planning for Deferred Employment Benefits**

#### **[§ 10.132]**

##### **A. In General [§ 10.133]**

Wisconsin's marital property law gives special treatment to deferred employment benefits. The term *deferred employment benefit* is defined in section 766.01(3m) as "a benefit from a deferred employment benefit plan." The term *deferred employment benefit plan* in turn is defined broadly in section 766.01(4) to include an arrangement under which compensation from employment is deferred until a later date or the happening of a future event. For a discussion of deferred-employment-benefit plans, see chapter 2, *supra*.

There are at least six aspects of deferred-employment-benefit plans that require that such plans be given special consideration in estate planning (although not all six necessarily apply to every deferred-employment-benefit plan). Several of these considerations also apply to

IRAs, although IRAs are not deferred-employment-benefit plans under the marital property law. *See supra* ch. 2.

First, the marital property law provides special classification rules for deferred employment benefits. *See* Wis. Stat. § 766.62; *see supra* ch. 2. However, as with other assets, the classification of deferred employment benefits can be altered by a marital property agreement. *See* Wis. Stat. § 766.17. In the estate planning process, the planner will confront two questions: (1) whether particular deferred employment benefits be classified in a marital property agreement; and, if so, (2) how they should be classified.

Second, a special survivorship rule, the *terminable interest rule*, applies to deferred employment benefits. Under the terminable interest rule, the nonemployee spouse's marital property interest in a deferred-employment-benefit plan terminates at the death of the nonemployee spouse if he or she predeceases the employee spouse. Wis. Stat. §§ 766.31(3), 766.62(5); *see supra* ch. 2. The same rule applies to an IRA if marital property assets in the IRA are traceable to the rollover of a deferred-employment-benefit plan. Wis. Stat. §§ 766.31(3), .62(5)(b). In the estate planning process, the planner will confront the question whether the terminable interest rule should be overridden by a provision in a marital property agreement with respect to a particular deferred-employment-benefit plan or rollover IRA. *See* Wis. Stat. § 766.58(7)(a). As discussed in section 10.136, *infra*, there is, in effect, a federal terminable interest rule that applies in the case of some deferred-employment-benefit plans governed by ERISA and that cannot be overridden by a marital property agreement. A related question in the case of IRAs not attributable to the rollover of a deferred-employment-benefit plan is whether a marital property agreement should affirmatively apply the terminable interest rule (IRAs are not deferred-employment-benefit plans and hence are not governed by the terminable-interest rule, with the exception of IRA assets that are traceable to the rollover of a deferred-employment-benefit plan). In the absence of a provision in a marital property agreement that treats all IRAs in the same manner relative to the terminable interest rule, a plan participant rolling benefits into an IRA should keep the rollover IRA segregated from any IRAs not traceable to a rollover from a deferred-employment-benefit plan to avoid a mixing issue.

Third, generally, deferred employment benefits are a form of deferred compensation for services that is not subject to income tax until the

benefits are ultimately paid to the employee or the employee's designated beneficiary. Thus, deferred employment benefits are worth less than 100 cents on the dollar to either the employee or the employee's beneficiary, because of the deferred income tax liability. This makes these assets a poor choice for funding a credit shelter trust since the deferred income tax liability will be borne by the trust and the portion of the applicable credit amount attributable to the income tax liability will be wasted. The deferred tax status of deferred employment benefits also gives rise to administrative and income tax issues if the nonemployee spouse dies first and the terminable interest rule does not apply (because it has been overridden by the terms of a marital property agreement) and when ERISA's preemption provisions do not apply.

Fourth, for most deferred-employment-benefit plans, and for IRAs (other than Roth IRAs), federal income tax law requires that distributions from the plan or account commence upon retirement or when the employee or account holder attains a specified age. These rules are extensive, complex, and beyond the scope of this book. For a discussion of planning for distributions from retirement plans and IRAs generally, *see* Price, *supra* § 10.1, at §§ 13.1–21.

Fifth, for certain deferred employment benefit plans governed by ERISA, the Retirement Equity Act of 1984 (REA) provides for certain mandatory benefits for a surviving spouse that can be waived only at certain times and only with the consent of the participant's spouse in accordance with the terms of the plan and ERISA. *See* I.R.C. § 417(a)(1), (2). Hence, irrespective of marital property law considerations, if the estate plan provides for benefits under a plan governed by REA to pass to anyone other than the participant's spouse, the technical requirements of the plan and federal law must be satisfied for there to be an effective waiver of the surviving spouse's federal rights in such retirement benefits.

Sixth, as a result of the U.S. Supreme Court's decision in *Boggs v. Boggs*, 520 U.S. 833 (1997), *see supra* ch. 2, the extent to which spouses may affect the distribution of assets held in a qualified plan governed by ERISA is limited. Because of the Court's conclusion that ERISA's anti-alienation provisions preempt state community property laws to the extent such laws would give the nonparticipant spouse a power of disposition over undistributed plan assets, marital property planning is restricted—but only as long as benefits are held in the plan. IRAs

established by individuals for their own benefit are not subject to the same restrictions.

## **B. ERISA Qualified Plans vs. Deferred Compensation Plans and Arrangements [§ 10.134]**

A detailed discussion of ERISA and deferred compensation plans and arrangements is beyond the scope of this book. For a discussion of planning for distributions from retirement plans and IRAs generally, see Price, *supra* § 10.1, at §§ 13.1–.21. For planning under the marital property law, however, qualified plans governed by ERISA should be distinguished from qualified plans not governed by ERISA and nonqualified plans.

As used in this chapter, the term *qualified plan* means an employer-sponsored plan qualified under I.R.C. § 401(a) that is also governed by ERISA. A trust created under such a plan is exempt from income taxation under I.R.C. § 501(a), and contributions to the plan are tax-deductible by the employer but not taxed to the employee until actually distributed. From an estate planning standpoint, it is important to recognize that qualified plans governed by ERISA are subject to the anti-alienation provisions of ERISA § 206(d) and I.R.C. § 401(a)(13) (in contrast, for example, to government plans or non-electing church plans, which may be qualified under I.R.C. § 401(a) but are exempt from the anti-alienation provisions under ERISA § 4(b)). In addition, qualified plans governed by ERISA are subject to REA's mandatory spousal benefit provisions.

The term qualified plan used in this chapter excludes nonqualified plans, IRAs, 403(b) tax-sheltered annuities and arrangements, and governmental and church plans. Thus, the term *qualified plan benefit* as used here is narrower than the term deferred employment benefit in section 766.01(3m), which includes, among others, qualified plans, SEP-IRAs, nonqualified plans, 403(b) arrangements, and governmental and church plans. Wis. Stat. § 766.01(3m), (4).

Marital property planning considerations with respect to qualified plans governed by ERISA are discussed in this section and sections 10.135–.45, *infra*; marital property planning considerations with respect to other deferred-employment-benefit plans are discussed at in sections 10.146–.147, *infra*.

## C. Qualified Plans Governed by ERISA [§ 10.135]

### 1. Classification Choices and Federal Preemption [§ 10.136]

As discussed in chapter 2, *supra*, although *Boggs v. Boggs*, 520 U.S. 833 (1997), leaves open whether ERISA preemption applies to assets distributed from a qualified plan, the probable answer is that it does not. Under the most logical reading of *Boggs*, ERISA merely preempts one right from the bundle of rights incident to community property—in this case, the predeceasing nonparticipant spouse’s power of disposition over assets in the plan (i.e., it imposes in effect a federal terminable interest rule with respect to undistributed plan assets). Hence, notwithstanding *Boggs*, it should be the case that assets in a qualified plan and assets distributed from a qualified plan have whatever classification state law provides, either by operation of law or, if applicable, pursuant to the terms of a marital property agreement. The holding in *Boggs* merely preempts state law to the extent it would allow a predeceasing nonparticipant spouse a power that is contrary to the purpose of ERISA.

Thus, from a planning standpoint, if spouses wish to adopt marital property generally as the classification of their assets, they could specify in a marital property agreement that the classification of assets as marital property extends to distributions from a deferred employment benefit plan governed by ERISA (note, however, that if qualified plan assets are rolled over to an IRA, further tax and nontax considerations should be considered and addressed). A provision in a marital property agreement generally classifying assets as marital property should be sufficient to achieve this result even without specific reference to plan distributions.

On the other hand, if spouses wish to adopt individual property generally as the classification of their assets (or for specific assets, including qualified plans), they could specify in a marital property agreement that the classification of assets as individual property extends to distributions from a deferred-employment-benefit plan governed by ERISA (note, however, that such classification will not preclude the applicability of the REA’s survivor benefits, which must be addressed specifically in accordance with the requirements of the plan and federal law. See I.R.C. § 417(a)(1), (2); *supra* ch. 7.

To the extent a participant's spouse is designated as the primary beneficiary of a plan's benefits, the classification of assets distributed from the plan to the surviving spouse upon the participant's death will be irrelevant. *See infra* § 10.143.

## **2. Death of Nonparticipant Spouse Before Participant Spouse [§ 10.137]**

### **a. In General [§ 10.138]**

Estate planning for spouses often includes estate tax planning designed to take maximum advantage of the applicable credit amount against estate taxes available to each spouse, which translates into a federal estate tax exclusion amount in 2004 and 2005 of \$1.5 million, with scheduled increases thereafter, a repeal year, and a sunset provision causing a reversion to the law as it existed prior to major tax cuts enacted in 2001. Wisconsin's "decoupled" estate tax, scheduled to be in effect through the end of 2007, limits the estate tax exclusion amount to \$675,000. See chapter 9, *supra* for a discussion of federal and Wisconsin estate tax laws. Whether the applicable credit amount can be fully utilized depends on the availability of assets over which the first spouse to die has a power of disposition. In many situations, spouses' assets are not evenly divided, and in some cases, a large part of the spouses' wealth is in the form of one of the spouse's retirement plan assets. In such a situation, if the nonparticipant spouse dies first, the question arises whether the nonparticipant spouse can dispose of a part of the participant spouse's plan assets by reason of a marital or community property interest. As discussed in section 10.140, *infra*, in the case of qualified plans governed by ERISA, such disposition is not possible, at least while assets are still in the plan.

### **b. Wisconsin Terminable Interest Rule [§ 10.139]**

Wisconsin's marital property law includes the terminable interest rule in the case of deferred-employment-benefit plans. Under the terminable interest rule, the nonemployee spouse's marital property interest in a deferred-employment-benefit plan terminates at the nonemployee spouse's death if he or she predeceases the employee spouse. Wis. Stat. §§ 766.31(3), 766.62(5). The terminable interest rule can be overridden

by a specific provision in a marital property agreement. *See* Wis. Stat. § 766.58(7)(a). However, as discussed below, such a provision would have no effect in the case of a qualified plan governed by ERISA in view of the *Boggs* decision.

### **c. Limitations Resulting from Boggs Decision** **[§ 10.140]**

The U.S. Supreme Court's decision in *Boggs v. Boggs*, 520 U.S. 833 (1997) is discussed in detail in chapter 2, *supra*. The effect of *Boggs* in the case of ERISA qualified plans is essentially the same as that of Wisconsin's terminable interest rule—that is, if the nonparticipant spouse predeceases the participant spouse, the nonparticipant spouse has no power of disposition (testamentary or otherwise) over the participant's qualified plan. Unlike the Wisconsin terminable interest rule, which can be overridden by a provision in a marital property agreement, *see* Wis. Stat. § 766.58(7)(a), spouses cannot contractually alter the effect of *Boggs* because of the anti-alienation provisions of ERISA.

Hence, unless assets held in a qualified ERISA plan are removed from the plan, those assets will be unavailable for planning in the context of the nonparticipant spouse's predeceasing the participant spouse. Depending on the provisions of the particular plan, there may be ways to remove assets from the plan. One way to remove assets from a qualified plan is to simply have them distributed to the participant. However, this will result in the recognition of ordinary income (in some cases involving employer-issued securities, the recognition will be limited, *see* I.R.C. § 402(e)(4)). To avoid recognizing income, the participant spouse can roll the assets from the qualified plan into an IRA held in his or her name, if the plan permits a lump-sum withdrawal. IRAs generally are not governed by ERISA and hence are not subject to the holding in *Boggs*. For a discussion of planning considerations in the context of an IRA when the spouse of the contracting party dies first, *see* sections 10.154–159, *infra*. Note that if the assets are rolled over into an IRA, the nonparticipant spouse will no longer have the survivor rights provided under REA. However, the remedy provisions of section 766.70 will nonetheless be available to the nonparticipant spouse with respect to his or her marital property interest if the nonparticipant survives the participant. The planner advising spouses in a joint representation



arrangement should discuss the impact of a decision to roll over assets from a qualified plan to an IRA with his or her clients.

### **3. Death of Participant Spouse Before Nonparticipant Spouse [§ 10.141]**

#### **a. In General [§ 10.142]**

Assets in a qualified ERISA plan pass at the death of the participant spouse in accordance with whatever beneficiary designation has been made by the participant, subject to the limitations of REA, as discussed below. In many instances, the participant's spouse is the logical beneficiary because of favorable provisions in the I.R.C. that permit a surviving spouse to roll over a distribution from a qualified plan into an IRA without having to recognize income at the time of the distribution. *See* I.R.C. § 408(d)(3)(C). In other instances, the spouse may not be the beneficiary, in which case both the limitations of the REA and the classification of the plan assets must be addressed.

#### **b. Surviving Spouse as Designated Beneficiary [§ 10.143]**

If the participant's spouse is to be the beneficiary of the qualified plan, the classification of the plan assets is of little consequence. The surviving spouse receives the benefits regardless of classification, and the assets received are IRD and thus are not eligible for a basis adjustment. *See* I.R.C. § 1014(c). In such instance there is no tax reason to include special provisions in a marital property agreement to classify the plan assets either as marital property or as individual property. If the spouses are entering into a marital property agreement, generally the best approach is to simply provide in the agreement that plan assets are classified as provided under the marital property law, so that the agreement does not purport to make any adjustment in the ownership rights of the spouses with respect to the plan assets.

**c. Surviving Spouse as Designated Beneficiary,  
with Disclaimer to Contingent Beneficiary  
Contemplated [§ 10.144]**

In some cases, spouses may want the surviving nonparticipant to be able to roll the plan benefits into an IRA and to be able to disclaim all or a portion of the benefits in favor of a contingent beneficiary (for example, a credit shelter trust). This might be the case, for example, if the ability to fully utilize the participant's applicable credit amount with non-IRD items were in question so that the survivor might choose to disclaim as a means of more fully utilizing the credit. In that situation, the classification of the plan assets should be considered. If the spouses want to give the survivor the flexibility to effect a qualified disclaimer of up to 100% of the plan assets in favor of the contingent beneficiary, the qualified plan should be classified as the participant's individual property, since the surviving spouse would not be able to make a qualified disclaimer of his or her own marital property interest. *See supra* ch. 9 (regarding qualified disclaimers). Note, however, that if the plan is reclassified as the participant's individual property, the nonparticipant no longer has a marital property interest in the assets. In addition, while the REA may protect the nonparticipant while assets are still in the plan, once the assets are distributed, that protection is gone (unless the distribution is made in the form of a joint and survivor annuity). *See* sections 10.20–.27, *supra*, for a discussion of considerations involved in adjusting the spouses' relative property rights to achieve shared tax and nontax objectives.

**d. Nonspouse as Designated Beneficiary  
[§ 10.145]**

If someone other than the spouse is to be the beneficiary of the qualified plan, the planner must consider both the REA spousal annuity rules and the classification of the qualified plan. Under the REA, for a beneficiary designation naming someone other than the spouse to be valid, the REA-mandated spousal annuity or death benefit provisions of the qualified plan must be waived by the participant and consented to by the spouse in accordance with the requirements of ERISA and the plan. *See* I.R.C. § 417(a)(1), (2). In addition, to avoid potential adverse gift or estate tax consequences, the qualified plan should be classified as the individual property of the participant. If it is not so classified (but rather

is classified in whole or in part as marital property), upon the participant's death the beneficiary designation becomes irrevocable and passes all of the benefits (including the surviving spouse's one-half marital property interest) to the designated beneficiary. If the surviving spouse fails to recover his or her interest from the beneficiary, he or she may be deemed to have made a gift to the extent of his or her interest. *See supra* ch. 9. Moreover, if the designated beneficiary of the qualified plan is a trust in which the survivor is a beneficiary, a portion of the trust may be included in the survivor's estate under I.R.C. § 2036 upon the spouse's later death. *See supra* ch. 9. Note, however, that if the plan is reclassified as the participant's individual property, the nonparticipant no longer has a marital property interest in the assets of the plan. See sections 10.20–27, *supra*, for a discussion of considerations involved in adjusting the spouses' relative property rights to achieve shared tax and nontax objectives.

#### **D. Nonqualified Plans and Arrangements Generally** **[§ 10.146]**

Many of the considerations applicable to planning for qualified plans, particularly those related to the terminable interest rule, are likewise applicable to planning for nonqualified plans and arrangements. However, in the case of nonqualified plans, the planner generally is not limited by ERISA's anti-alienation provisions and hence there may be more flexibility in planning for the disposition of the nonparticipant spouse's marital property interest if he or she dies first. In that regard, many of the same considerations applicable to planning for IRAs are applicable in planning for nonqualified plans. See sections 10.154–159, *infra*, for a discussion of planning for disposition of the noncontracting spouse's marital property interest in an IRA if he or she dies first. In addition, in the case of nonqualified plans, the REA's mandatory spousal benefit provisions generally are not applicable. This may give the participant spouse more flexibility in directing the disposition of plan benefits at death (subject, however, to the surviving spouse's remedies in the case of benefits classified as marital property and not paid to the survivor).

Nonqualified plans vary widely in structure and terms. Before adopting a particular strategy for the disposition of benefits under a nonqualified plan, it may be helpful for the planner to obtain and review a copy of the employee's contract or other governing plan document.

This may disclose relevant provisions such as an anti-assignment provision precluding the participant from making certain transfers or may affect the amount of benefits payable under different circumstances (such as death, disability, termination of employment, etc.). Such a contractual prohibition should not affect the spouses' ability to adopt a particular classification for the plan benefits, but the terms of the contract with the participant's employer will continue to control timing and amount of distributions. This is true even if the nonparticipant spouse dies first owning a marital property interest, the terminable interest rule having been overridden by the terms of a marital property agreement.

Hence, subject to a review of the applicable plan provisions, the basic considerations in planning for nonqualified plans and arrangements are: (1) the participant spouse may designate the beneficiary of his or her choice, but if he or she dies first and the surviving nonparticipant spouse is not named as the beneficiary, the survivor may have a remedy to the extent of the survivor's marital property interest, *see Jackson v. Employee Trust Funds Bd.*, 230 Wis. 2d 677, 602 N.W.2d 543 (Ct. App. 1999) (discussed at section 10.147, *infra*); (2) if the existence of such a remedy by the surviving nonparticipant spouse is undesirable for tax planning or other reasons, the classification of the plan can be addressed in a marital property agreement; (3) if the nonparticipant spouse dies first, he or she has no power of testamentary disposition over any marital property interest in the plan on account of the terminable interest rule, unless the rule has been overridden by specific provisions in a marital property agreement; and (4) if the spouses wish to override the terminable interest rule so that the nonparticipant has a power of testamentary disposition, this must be accomplished by marital property agreement, but this planning strategy has limited application in joint tax planning.

### **E. State of Wisconsin Retirement System [§ 10.147]**

As noted in chapter 2, *supra*, the Department of Employee Trust Funds early on issued a document suggesting that chapter 766 had no application to Wisconsin Retirement System (WRS) benefits. However, in *Jackson v. Employee Trust Funds Board*, 230 Wis. 2d 677, 602 N.W.2d 543 (Ct. App. 1999), the court noted the parties' lack of dispute on the application of section 766.62(1)(a) to the WRS benefits at issue. The issue in the case was whether the department was prohibited by chapter 766 from giving effect to the deceased wife's beneficiary designation, which named her sister as beneficiary to the exclusion of her surviving

husband, who claimed a marital property interest in the benefits. The court concluded that the department had no obligation to consider the potential marital property rights of the surviving spouse, noting that the remedy provisions under section 766.70 allow a surviving spouse to enforce a claim to his or her share of marital property assets passing to a third party.

ERISA does not apply to government retirement plans such as the WRS. Hence, the mandatory spousal benefit provisions of the REA do not apply. Nor does *Boggs v. Boggs*, 520 U.S. 833 (1997), which held that federal law preempts state community property law to the extent it gives a predeceasing nonparticipant spouse a power of disposition over assets in a qualified plan. Note, however, that because a WRS plan is a deferred-employment-benefit plan under section 766.01(4), the terminable interest rule of sections 766.31(3) and 766.62(5) applies unless overridden by specific provisions in a marital property agreement. Many of the same considerations applicable to planning for IRAs are applicable to planning for WRS benefits. See sections 10.148–.160, *infra*, for a discussion of planning for IRAs.

## **XIV. Planning for IRAs [§ 10.148]**

### **A. Classification and Federal Preemption [§ 10.149]**

With the exception of SEP-IRAs, IRAs are not deferred-employment-benefit plans under section 766.01(4). See *supra* ch. 2. As a result, the special classification rules for deferred-employment-benefit plans under section 766.62 do not apply to IRAs; rather, the general classification rules of section 766.31 apply to IRAs. However, if the assets in an IRA are traceable to the rollover of a deferred-employment-benefit plan, the terminable interest rule applies. Wis. Stat. §§ 766.31(3), .62(5). Given this different treatment for IRAs whose assets are traceable to a rollover from a deferred-employment-benefit plan, it is advisable to avoid mixing rollover and nonrollover IRAs. For a discussion of the terminable interest rule, see chapter 2, *supra*.

Several considerations applicable in planning for deferred employment benefits apply to IRAs as well. For traditional IRAs (in contrast to Roth IRAs, discussed at section 10.157, *infra*), federal income tax law requires that distributions from the IRA commence when the account holder attains a specified age. These rules are extensive,

complex, and beyond the scope of this book. For a discussion of estate planning for retirement plans and IRAs generally, see Price, *supra* § 10.1, at §§ 13.1–.21.

Although the tax-qualified nature of IRAs is determined by federal law, the management and disposition of IRAs is a matter of state law. To be federally tax qualified, an IRA must be either a trust, *see* I.R.C. § 408(a), or a custodial account, *see* I.R.C. § 408(h). In either case, to be qualified for federal tax purposes the governing instrument must include certain provisions and must be administered in accordance therewith. However, the property rights created by the trust or custodial arrangement are a matter of state law and are not governed by ERISA. The spousal benefit requirements imposed by the REA, discussed in section 10.32, *supra*, are not applicable to IRAs. Moreover, the most logical reading of the *Boggs* decision, *see supra* ch. 2, limits the holding regarding preemption of state community property laws to “undistributed pension plan benefits” and thus is not by its terms applicable to IRAs (although dicta in *Boggs* may suggest otherwise). The IRS has recognized in a number of private rulings that an IRA may be composed in whole or in part of community property. *See, e.g.*, Priv. Ltr. Rul. 8040101 (July 15, 1980) (concluding that classification of IRA interest is question of state law); Priv. Ltr. Rul. 9234014 (Aug. 21, 1992) (approving apportionment of community property IRAs between spouses); Priv. Ltr. Rul. 9321035 (May 28, 1993) (involving division of community property IRA between decedent’s surviving spouse and QTIP trust); Priv. Ltr. Rul. 9427035 (July 8, 1994) (survivor’s interest in community property IRA allocable to revocable survivor’s trust was directly transferred to new IRA of survivor as qualified rollover); Priv. Ltr. Rul. 9439020 (Sept. 30, 1994) (agreement to divide community property IRA into two separate property IRAs not a distribution); Priv. Ltr. Rul. 9630034 (July 26, 1996) (involving qualified disclaimer by wife of husband’s portion of community property IRA); Priv. Ltr. Rul. 9633043 (Aug. 16, 1996) (surviving spouse deemed beneficiary as to her community property interest in IRA for purposes of qualified rollover); Priv. Ltr. Rul. 9937055 (Sept. 17, 1999) (acknowledging marital property interest of spouse in IRA by virtue of marital property agreement and concluding that reclassification of IRA as marital property by agreement is not considered a taxable distribution under I.R.C. § 408(d)(1)).

Moreover, state court decisions in other jurisdictions have recognized the community property ownership rights of spouses in IRAs when the noncontracting spouse dies first. *See Estate of MacDonald v.*

*MacDonald*, 794 P.2d 911 (Cal. 1990); *In re Estate of Mundell*, 857 P.2d 631 (Idaho 1993) (children of deceased husband successful in claiming husband's one-half community property interest in surviving wife's IRA). The state of Washington expressly recognizes, by statute, the community property rights of a noncontracting spouse in a community property IRA, including his or her right to dispose of that interest by will. Wash. Rev. Code § 6.15.020 (2004). In Wisconsin, if an IRA is not subject to the terminable interest rule, it likewise should be the case that the predeceasing noncontracting spouse has a testamentary power of disposition over one-half of the marital property interest in the IRA.

Thus, while there are similarities in planning for qualified plans and IRAs (due to their similar minimum-distribution requirements and their deferred-income status), given the absence of ERISA preemption of state community property rights and the absence of the REA's spousal annuity rights, there are significant differences as well.

## **B. Contracting Spouse Dies First [§ 10.150]**

### **1. Surviving Spouse as Designated Beneficiary [§ 10.151]**

If the contracting party with respect to an IRA designates his or her spouse as the beneficiary of the IRA, the classification of the IRA is of little consequence if the spouse survives. At the contracting spouse's death, the surviving spouse receives the IRA assets regardless of their classification, and the assets received are IRD and thus are not eligible for a basis adjustment. *See* I.R.C. § 1014(c). In that instance there is no tax reason to include special provisions in a marital property agreement to classify the IRA either as marital property or as individual property. If the spouses are entering into a marital property agreement, generally the best approach is to simply provide in the agreement that the IRA is classified as provided under the marital property law, so that the agreement does not make any adjustment in the spouses' ownership rights with respect to the IRA.

## **2. Surviving Spouse as Designated Beneficiary, with Disclaimer to Contingent Beneficiary Contemplated [§ 10.152]**

In some cases, spouses may want the surviving noncontracting spouse to be able to roll the contracting spouse's IRA proceeds into an IRA and to be able to disclaim all or a portion of the IRA assets in favor of a contingent beneficiary (for example, a credit shelter trust). This might be the case, for example, if the ability to fully utilize the noncontracting spouse's applicable credit amount with non-IRD items were in question so that the survivor might choose to disclaim as a means of more fully utilizing the credit. In that situation, the classification of the IRA assets should be considered. If the spouses want the survivor to be able to effect a qualified disclaimer of up to 100% of the IRA assets in favor of the contingent beneficiary, the IRA should be classified as the contracting spouse's individual property, since the surviving spouse would not be able to disclaim his or her marital property interest. Note, however, that if the IRA is reclassified as the contracting spouse's individual property, the noncontracting spouse no longer has a property interest in the asset (however, there may be "property rights" under the trust or custodial agreement in the absence of a valid beneficiary designation). See sections 10.20–.27, *supra*, for a discussion of the considerations involved in adjusting the spouses' relative property rights to achieve shared tax and nontax objectives.

## **3. Nonspouse as Designated Beneficiary [§ 10.153]**

If someone other than the contracting party's spouse is to be the beneficiary of an IRA, the planner must consider the IRA's classification. To avoid potential adverse gift or estate tax consequences, the IRA should be classified as the contracting spouse's individual property. If it is not so classified (but rather is classified in whole or in part as marital property), upon the contracting spouse's death the beneficiary designation becomes irrevocable and passes all of the benefits (including the surviving spouse's one-half marital property interest) to the designated beneficiary. If the surviving spouse fails to recover his or her interest from the beneficiary, he or she may be deemed to have made a gift to the extent of his or her interest. Moreover, if the designated beneficiary of the IRA is a trust of which the survivor is a beneficiary, a portion of the trust may be included in the survivor's estate



under I.R.C. § 2036 upon the survivor's later death. *See supra* ch. 9. Note, however, that if the IRA is reclassified as the contracting spouse's individual property, the noncontracting spouse no longer has a property interest in the asset (however, there may be "property rights" under the trust or custodial agreement in the absence of a valid beneficiary designation). See sections 10.20–27, *supra*, for a discussion of the considerations involved in adjusting the spouses' relative property rights to achieve shared tax and nontax objectives.

## **C. Noncontracting Spouse Dies First [§ 10.154]**

### **1. Certain IRAs Subject to Terminable Interest Rule [§ 10.155]**

If the assets in an IRA are traceable to the rollover of a deferred-employment-benefit plan, the terminable interest rule applies. Wis. Stat. §§ 766.31(3), .62(5). For a discussion of the terminable interest rule, see chapter 2, *supra*. If the noncontracting spouse dies before the contracting spouse, the noncontracting spouse has no power of disposition over the portion of the contracting spouse's IRA classified as marital property unless the terminable interest rule has been overridden by a provision in a marital property agreement.

### **2. IRAs Not Subject to Terminable Interest Rule [§ 10.156]**

#### **a. Alternative Dispositions of Noncontracting Spouse's Interest [§ 10.157]**

If the assets of an IRA are classified in whole or in part as marital property and are not traceable to the rollover of a deferred-employment-benefit plan, the terminable interest rule does not apply to the IRA. Moreover, spouses may agree in a marital property agreement to expressly override the terminable interest rule even when assets of an IRA are traceable to the rollover of a deferred-employment-benefit plan. *See* Wis. Stat. § 766.58(7)(a). In either case, if the noncontracting spouse predeceases the contracting spouse, the deceased spouse's marital property interest in the IRA is subject to disposition under the deceased spouse's will (or intestate succession rules). *See supra* §§ 10.154–159.

If the surviving spouse (the contracting party) is named as the beneficiary of the deceased spouse's interest (either as a specific legatee or as residuary beneficiary under the deceased spouse's will, or by intestate succession), as a practical matter, there will be no change in ownership of the IRA.

On the other hand, if the terminable interest rule does not apply to an IRA, the noncontracting spouse dies first, and the deceased spouse's marital property interest in the IRA passes under his or her will to someone other than the surviving spouse, a more complicated analysis ensues. It should first be noted that this result, which is probably not desirable, can be avoided through planning. One alternative would be to classify the IRA as the individual property of the contracting spouse. This will eliminate any power of testamentary disposition over the IRA by the noncontracting spouse if he or she dies first, but it will also eliminate the noncontracting spouse's ownership rights in the IRA. If the IRA is classified as individual property, the contracting spouse is free to designate any beneficiary he or she chooses, and the surviving noncontracting spouse has no remedy if the designation makes no provision for him or her. In some instances this may be necessary—when, for example, the adopted plan contemplates the contracting spouse designating a child or a credit shelter trust as the beneficiary of the IRA; in that case, individual property classification is necessary to avoid adverse gift tax or estate tax consequences for the surviving spouse or the surviving spouse's estate.

When adopting individual property classification is unnecessary for planning purposes, however, the noncontracting spouse's power of testamentary disposition can be eliminated by having the spouses include in a marital property agreement a provision stating that all IRAs will be treated as if traceable to the rollover of a deferred-employment-benefit plan (thereby imposing the terminable interest rule). This eliminates any power of testamentary disposition by the noncontracting spouse, but if the noncontracting spouse is the survivor, any marital property rights in the IRA remain intact.

There may be instances in which the spouses do not want the terminable interest rule to apply to an IRA, even one that is traceable to the rollover of a deferred-employment-benefit plan. This may be the case, for example, if the spouses' assets are unbalanced and there are insufficient other assets over which the noncontracting spouse has a power of disposition at death, thereby placing the spouses at risk of

“wasting” the opportunity to fully fund a credit shelter trust if the noncontracting spouse dies first.

➤ **Example.** Wisconsin domiciled spouses have two assets, a house owned as survivorship marital property, valued at \$600,000, and the husband’s IRA, valued at \$3 million. The assets of the IRA are traceable to the rollover of a qualified plan. Neither spouse has used any part of his or her applicable credit amount.

This example highlights the planner’s dilemma. On the one hand, if each spouse’s credit can be fully utilized, the amount subject to estate tax in the survivor’s estate can be greatly reduced. On the other hand, it is not possible to know which spouse will die first or when, and, in any event, to achieve the intended full use of each spouse’s applicable credit amount, it will be necessary to use the IRA in part. As an IRD asset, the IRA is worth less than 100 cents on the dollar and therefore is generally not the best asset for funding a credit shelter trust. In the example, however, it is the only available asset, other than the house, to fund a credit shelter trust.

The course of action ultimately adopted by the spouses in the example depends on their intentions and how they prioritize those intentions. It is likely that one of their goals will be to provide for the survivor and that another will be to provide for children in a tax-efficient manner following the survivor’s death. However, the best estate tax planning result (which will benefit the children) may compromise the best course of action to benefit and protect the surviving spouse (i.e., leaving assets in the husband’s IRA, or in the wife’s rollover IRA, as long as possible). Thus there is no one “right” solution to the planning dilemma, but rather a number of trade-offs to be considered, with the result in each case driven by the spouses’ priorities.

If the spouses’ priority in the example is to maximize the benefits available to the survivor, the husband would designate the wife as the primary beneficiary of the IRA with a credit shelter trust (of which the spouse is the primary beneficiary) named as the contingent beneficiary. No special provisions regarding the IRA would need to be included in a marital property agreement (even if classified 100% as marital property, the predeceasing contracting spouse’s one-half interest, valued at \$1.5 million, could be the subject of a qualified disclaimer). If the husband died first, the wife could roll over the IRA proceeds (both her own one-half interest and her husband’s) into her own IRA. Alternatively, the

wife could disclaim part or all of the husband's marital property interest in the IRA and allow that interest to pass to the contingent beneficiary (whether the wife would choose this alternative would depend on the circumstances at the time). If the wife in the example died first, the terminable interest rule would terminate her marital property interest in the IRA. Thus, the IRA would belong solely to the surviving husband, and no part of the IRA would be available to fund the credit shelter trust (the planning might also include reclassifying the residence as the wife's individual property to have a significant asset with which to fund the credit shelter trust in the event she were to predecease her husband).

On the other hand, if the spouses in the example conclude that their priority is to minimize estate taxes, more aggressive planning involving the husband's IRA could be considered to allow more full utilization of each spouse's applicable credit amount. The spouses could agree by marital property agreement that the IRA (1) is marital property and (2) is not governed by the terminable interest rule. *See* Wis. Stat. § 766.58(7)(a); *see supra* §§ 10.154–.155 (regarding overriding the terminable interest rule by marital property agreement). If the terminable interest rule were overridden and the wife died first, the provisions of her will would control the disposition of her one-half marital property interest in the IRA, although there are questions about the timing and income taxation of such disposition. In Private Letter Ruling 80-40-101 (July 15, 1980), the IRS allowed the noncontracting spouse's community property interest in the contracting spouse's IRA to be distributed in accordance with the terms of the noncontracting spouse's will and further concluded that the resulting distribution would be taxed to the recipients (and not to the surviving contracting spouse). Under the ruling, the IRA custodian was able to recognize the probate court's order to distribute the deceased spouse's interest in the IRA to the beneficiaries designated in the deceased spouse's will.

In the example, to reserve a “second look” and the opportunity for IRS approval of the testamentary disposition of the wife's one-half marital property interest to a credit shelter trust, the wife's will could contain a specific bequest of her interest in the IRA to the husband, with the husband having the right to disclaim in favor of the credit shelter trust. If the wife died first and the husband were inclined to disclaim the bequest in whole or in part, the personal representative of the wife's estate could seek a ruling from the IRS regarding the tax consequences of the proposed disclaimer before committing to that course of action.

A possible alternative to waiting until the death of one spouse would be to seek IRS approval for a “partition” of the contracting spouse’s IRA. In Private Letter Ruling 94-39-020 (July 7, 1994), the IRS considered whether a taxpayer’s community property IRA could be “partitioned” into separate equal shares within the contracting spouse’s IRA, with one share subject to disposition by each spouse. Under the facts of the ruling, the spouses intended to enter into an agreement pursuant to which the IRA would be divided equally between them with each spouse’s share thereafter being owned as separate property, and with each spouse having the right to designate the beneficiary of his or her share. Each spouse intended to revocably designate the other as beneficiary of his or her share, with the survivor having the right to disclaim in favor of a testamentary trust. The IRS concluded: “Such reclassification, alone, is not tantamount to an actual distribution or payment from an IRA. Furthermore, such reclassification will not cause the IRA to fail to meet the requirements under section 408(a) so as not to be for the exclusive benefit of the involved taxpayer(s).” The IRS hence concluded that the partition was not a taxable event.

The term *partition* used in the ruling appears to mean a contractual reclassification from community property to separate property by agreement. Although the term partition is not typically used this way in Wisconsin, the same technique should be available to Wisconsin spouses. It should further be noted that Private Letter Ruling 94-39-020 does not address the income tax consequences of the distribution of the noncontracting spouse’s interest in the IRA if he or she were to die first. Requesting a ruling on this aspect of the proposed transaction would be advisable.

➤ **Note.** It must be emphasized that this type of planning is appropriate for joint tax planning only in those circumstances, such as in the example above, in which there are insufficient assets with which to plan for use of the noncontracting spouse’s applicable credit amount and the only reasonable alternative is to use the contracting spouse’s significant IRA assets as a potential source of funding for the credit shelter trust if the noncontracting spouse dies first.

In Private Letter Ruling 9937055 (Sept. 17, 1999), the IRS concluded that a lifetime transfer of a noncontracting spouse’s marital property interest to her own IRA would constitute a taxable distribution under I.R.C. § 408(d)(1). This is consistent with the U.S. Tax Court’s rulings

in *Rodoni v. Commissioner*, 105 T.C. 29 (1995), and *Bunney v. Commissioner*, 114 T.C. 259 (2000).

### **b. Mechanics of Disposition and Income Tax Issues [§ 10.158]**

If the noncontracting spouse dies first and the contracting spouse's IRA is not subject to the terminable interest rule, the noncontracting spouse has a power of testamentary disposition over one-half of the portion of the IRA classified as marital property. If the contracting spouse is named as the beneficiary under the noncontracting spouse's will (either by way of a specific bequest of the noncontracting spouse's marital property interest in the IRA or as the residuary beneficiary), the deceased spouse's interest will remain in the IRA and hence there should be no income tax consequences to the disposition. Moreover, the deceased spouse's interest arguably remains exempt from creditor claims pursuant to the exemption afforded retirement benefits under section 815.18(3)(j).

If, on the other hand, the contracting spouse is not the beneficiary under the noncontracting spouse's will with respect to the noncontracting spouse's marital property interest in the IRA (for example, if the noncontracting spouse's will pours over to a residuary trust, or if the contracting spouse disclaims a specific bequest of the noncontracting spouse's interest in the IRA in favor of a credit shelter trust), the analysis is more complicated.

The initial question in that instance is how the personal representative of the noncontracting spouse's estate asserts a claim of right to the decedent's interest in the contracting spouse's IRA. If the contracting spouse's IRA is a trust (*see* I.R.C. § 408(a)), section 766.575, relating to the protection of trustees dealing with spouses, provides the mechanism. Section 766.575(2) provides:

Except as provided in sub. (3), in a court order or in the terms of a trust, the classification of property in the possession or control of a trustee shall not affect the trustee's right and duty to administer, manage and distribute the property in accordance with the terms of the governing instrument and the trustee may rely on and act in accordance with those terms.

Subsection (3) goes on to specify a notice of claim procedure that may be used by a surviving spouse, or by a person claiming under a deceased spouse's disposition at death, to establish a claim to a portion of the assets held in the trust. Section 766.575 does not address the timing of distributions from the trust in satisfaction of a claim established pursuant to the notice of claim procedure.

If the contracting spouse's IRA is a custodial account, *see* I.R.C. § 408(h), rather than a trust, section 766.575 technically may be inapplicable. Section 766.575(1)(e) defines *trustee* by cross-reference to section 701.01(8), which in turn defines trustee to mean "a person holding in trust title to or holding in trust a power over property." A custodian of an IRA qualified under I.R.C. § 408(h) may not be considered a trustee under this definition. Nonetheless, a custodian receiving a notice of claim similar to the one contemplated in section 766.575(3) would be well advised to seek direction from the probate court regarding the disposition of IRA assets.

Whether the IRA is a trust or a custodial account, the marital property component of the account may be established by a proceeding to determine the classification of property pursuant to section 857.01. The relief sought under section 857.01 may (though need not) include a decree requiring that property be titled in accordance with its classification.

With respect to income tax consequences when the contracting spouse is not the beneficiary of the noncontracting spouse's marital property interest in the IRA, some commentators have suggested that the result may be current income taxation of the decedent's marital property interest, and, in some circumstances, imposition of the 10% excise tax imposed by I.R.C. § 72(t) on premature distributions if the surviving contracting spouse has not attained age 59½. *See, e.g.,* S. Andrew Pharies, *Community Property Aspects of IRAs and Qualified Plans*, Prob. & Prop. Sept./Oct. 1999 at 33, 37–38. This analysis assumes, however, that the noncontracting spouse's marital property interest in the contracting spouse's IRA is distributed because of the noncontracting spouse's death. A more practical approach may be to obtain an order from the probate court directing the IRA trustee or custodian to make payments to the noncontracting spouse's beneficiary as distributions are made in accordance with the surviving contracting spouse's continued exercise of management and control rights with respect to the IRA. Given the uncertainty of the income tax results, however, the surviving

spouse or personal representative of the deceased spouse may wish to obtain a private ruling from the IRS regarding the income tax consequences of this approach.

➤ **Note.** If the noncontracting spouse dies first and has a power of testamentary disposition over the contracting spouse's IRA, the contracting spouse should not make additional contributions to that IRA. Rather, any IRA contributions made by the surviving spouse following the death of the noncontracting spouse should be made to a different IRA to avoid mixing issues.

### **c. Non-Pro Rata Distribution [§ 10.159]**

Two private letter rulings suggest that use of non-pro rata distributions following death may facilitate funding a credit shelter trust using the value of spouses' marital property interest in an IRA. In both Private Letter Ruling 99-25-033 (June 25, 1999) and 99-12-040 (December 18, 1998), the deceased spouse's IRA was owned as community property and was payable upon death to the spouses' joint revocable trust. Under the facts of each ruling, the trustees proposed to allocate the entire amount of the IRA proceeds (both the one-half community property interest of the decedent and the one-half community property interest of the surviving spouse) to the survivor's trust and to allocate the entire interest in other community property assets of equal value (determined as of dates of distribution) exclusively to the decedent's one-half share of the former community property. In both rulings, the IRS ruled that the non-pro rata distribution was not a sale or exchange under I.R.C. § 1001. In both cases, local law and the governing trust instrument authorized non-pro rata distributions. Finally, in each ruling, the surviving spouse rolled the IRA proceeds into the survivor's own IRA without recognition of income.

Planners wishing to follow the planning strategy described in these rulings should include a provision in the governing trust instrument authorizing non-pro rata distributions. Even if such provision is absent, however, Wisconsin law specifically authorizes non-pro rata distributions by way of exchanging marital property assets following death, albeit with court approval in the probate context. *See* Wis. Stat. § 857.03(2). 2005 Wisconsin Act 216, section 169, renumbered section 857.03(2) as section 766.31(3)(b)3. and amended the statute to



coordinate its provisions with changes made by 2005 Wisconsin Act 216, section 42, discussed in section 10.10, *supra*.

Although the above rulings involved situations in which the contracting spouse died first, the non-pro rata distribution strategy may have application when the noncontracting spouse dies first. The steps would include the following:

1. The spouses classify an IRA as marital property (and as necessary override the terminable interest rule by provisions in their marital property agreement).
2. The noncontracting spouse by will specifically bequeaths any marital property interest in the contracting spouse's IRA to the contracting spouse, with a provision permitting the contracting spouse to disclaim in favor of his or her estate.
3. The will further provides that, to the extent possible, any interest of the decedent in the surviving spouse's IRA will be allocated to the surviving spouse as part of a non-pro rata distribution of the estate assets.
4. If the noncontracting spouse dies first, the surviving spouse disclaims the amount necessary to fund the credit shelter trust. The IRA could then be allocated back to the surviving spouse in a non-pro rata distribution in exchange for the surviving spouse's interest in other marital property assets.

As in the above-cited private letter rulings, the non-pro rata distribution should not be regarded as a sale or exchange. Of course, the cited rulings are limited to the taxpayers to whom they were issued and therefore do not serve as precedent. A provision authorizing non-pro rata distributions is not necessary if they are permitted by governing state law. *See, e.g.*, Priv. Ltr. Rul. 2003-34-030 (May 19, 2003) (non-pro rata distribution of assets upon the termination of a trust did not involve recognition of gain or loss because the divisions were authorized by state law). For further discussion of this issue, see section 9.20, *supra*.

## **D. Roth IRAs [§ 10.160]**

Unlike a traditional IRA, the distributions from which are subject in whole or in part to income taxation in all events at some point in the future, a Roth IRA established by a qualifying taxpayer (by way of nondeductible contributions or a qualified conversion) can ultimately be distributed to the taxpayer or his or her beneficiary free of income tax if the distributions satisfy certain requirements. For a discussion of Roth IRAs and the rules that govern contributions, conversions, and distributions, see generally Mervin M. Wilf, “Roth IRAs: Distribution Planning Issues Arising from the Final Regulations and Other Guidance,” Q284 ALI-ABA 121 (1999). Unlike traditional IRAs, during the contracting spouse’s lifetime, minimum distribution rules do not apply to Roth IRAs (though such rules apply following the death of the contracting spouse). *See* I.R.C. § 408A(c)(5).

Because a Roth IRA, unlike a traditional IRA, is not an item of IRD, a Roth IRA is a more suitable asset for funding a credit shelter trust. As with any asset that is earmarked to pass to a credit shelter trust, the planner must consider its classification. The same considerations applicable to a traditional IRA that may be used to fund a credit shelter trust are applicable to a Roth IRA that will serve that purpose. *See supra* § 10.159. If an estate plan contemplates that a Roth IRA will fund a credit shelter trust upon the contracting spouse’s death, classification of the Roth IRA as the contracting spouse’s individual property will make it possible for the entire Roth IRA to pass to the credit shelter trust without adverse gift tax or estate tax consequences for the surviving spouse or the surviving spouse’s estate.

The considerations for disposition of a Roth IRA classified as marital property upon the death of the noncontracting spouse are essentially the same as those for a traditional IRA. Whether a Roth IRA may be “partitioned” in the same manner as a traditional IRA is untested.

## **XV. Alternatives in Representing One Spouse [§ 10.161]**

### **A. In General [§ 10.162]**

While in most cases spouses will retain the same counsel in a joint representation relationship for their estate planning, in some cases the

planner may be advising only one spouse, whose objectives may include minimizing the impact the marital property law has on the other spouse's ability to assert property rights. This circumstance may arise, for example, following the representation of a spouse or prospective spouses in connection with an opt-out form of marital property agreement. Sections 10.160–.167, *infra*, consider some of the issues and strategies that may be applicable in the context of such sole representation.

## **B. Opt-out (or Partial Opt-out) Marital Property Agreements [§ 10.163]**

Wisconsin's marital property law is based on a partnership theory of marriage, in which the contribution of each spouse to the marriage and the spouses' mutual responsibilities are recognized in the presumption that assets acquired by either spouse are classified as marital property. *See supra* ch. 1. At the same time, however, chapter 766 recognizes that spouses are free to adopt their own property regime, with limited exceptions. Wis. Stat. § 766.17. For counsel representing only one spouse, the principal means to effect that spouse's ability to exercise exclusive ownership rights with respect to an asset, both during lifetime and upon the death of either spouse (or in the event of the marriage's dissolution), is a marital property agreement. For a discussion of planning considerations with respect to marital property agreements, including drafting considerations, see chapter 7, *supra*.

## **C. Unilateral Actions to Preserve Classification of Nonmarital Property Assets [§ 10.164]**

### **1. Segregation and Tracing of Nonmarital Property Assets [§ 10.165]**

A spouse who owns assets not classified as marital property (for example, predetermination date property assets or individual property assets acquired by gift or transfer upon death) must be disciplined in segregating and accounting for such assets to avoid the inadvertent reclassification of part or all of them as marital property. Further, even if a marital property agreement is in place that classifies spouses' assets generally as individual property, the agreement's effect on a creditor is limited by section 766.55(4m). Hence, notwithstanding the agreement, a

spouse concerned about potential creditor claims may be well advised to segregate and account for assets on a dual basis—that is, both as if there were a marital property agreement in place and as if there were not. This would involve keeping property classified as individual property under the agreement segregated from property classified as marital property under the agreement, and then further segregating the individual property assets that would be classified as individual property absent the agreement from those that would be classified as marital property absent the agreement.

In addition, given the differences between the manner in which property is characterized as either divisible or nondivisible under chapter 767, which governs dissolution, and the manner in which property is classified as either marital property or individual property under chapter 766, which governs classification of property during marriage and upon death, the spouse concerned about possible divorce should be mindful of the rules under both chapters.

➤ **Example.** At the time of his marriage in 1986 (when both spouses are domiciled in Wisconsin), a husband has significant assets, including a substantial bank account, the source of which was savings from premarriage employment. Upon marriage, he signs and delivers to his wife a unilateral statement under section 766.59. The husband thereafter is careful to avoid adding funds to the account that represent earnings from employment after the date of marriage. In 1988, the husband inherits significant assets from his mother. Since these assets, like the assets in his individual property bank account, are also classified as individual property, the husband commingles his inherited individual property funds with his premarriage individual property funds, and makes a number of withdrawals from the account and deposits of other premarriage funds. In 2010, the spouses file a petition for dissolution.

In the example, while the facts show that the entire account is classified as individual property under chapter 766, the division of property upon dissolution is governed by chapter 767. Chapter 767 generally treats as nondivisible only property acquired by gift or transfer at death from a third party. Wis. Stat. § 767.61. Income from nondivisible property is divisible. *See infra* ch. 11. The unilateral statement is a vehicle recognized under chapter 766, but not under chapter 767. Moreover, while the fact that property was owned by a spouse before the marriage is a factor for a court to consider in

determining an equitable distribution of property at divorce, *see* Wis. Stat. § 767.61(3)(b), premarriage property not attributable to a gift or transfer at death is part of the divisible marital estate. The husband has the burden of identifying and tracing the nondivisible assets, which, under the facts in the example, will be quite difficult.

The point, therefore, is that careful segregation and accounting to reflect classification solely under chapter 766 may be insufficient in many instances to provide the level of segregation and accounting necessary to adequately identify and trace assets for purposes of chapter 767, unless a marital property agreement is in place that in effect adopts the property classification scheme under chapter 766 as the means for dividing property in the event of divorce. And even when there is such a marital property agreement in place, out of an abundance of caution (because of the potential unenforceability of the agreement), a spouse may wish to also segregate and account for property as if there were no agreement.

A revocable trust may be a useful means of segregating and accounting for nonmarital property assets. It should be noted, however, that merely transferring property to a revocable trust does not suspend the classification rules under chapter 766 or the characterization rules under chapter 767. Hence, to the extent a dual system of segregation and accounting is advisable under circumstances like those in the example above, such segregation and accounting should be accomplished by the use of separate accounts within the revocable trust.

## **2. Unilateral Statement [§ 10.166]**

A spouse may unilaterally cause the income from nonmarital property to be classified as individual property by executing and delivering a unilateral statement under section 766.59 to his spouse (or prospective spouse). A unilateral statement is effective for purposes of chapter 766 as between the spouses, but it has no application in determining the division of property upon divorce under chapter 767, and its effect with respect to creditors is limited by the provisions of sections 766.55(4m) and 766.59(5).

### 3. Payment of Reasonable Compensation for Application of Labor to Nonmarital Property Assets [§ 10.167]

Under section 766.63(2), the so-called *industry mixing* or *labor mixing* provision, a marital property component may be created in a nonmarital property asset if the property substantially appreciates as a result of the application of substantial effort by either spouse when that spouse does not receive reasonable compensation for his or her effort. A spouse who owns a nonmarital property asset (for example, inherited stock in a family business) should ensure that either spouse working in the business receives reasonable compensation for services.

What constitutes *reasonable compensation* for purposes of section 766.63(2) will depend on the facts and circumstances of the particular case. The most conservative approach to rebuffing a challenge by the other spouse or a third party (e.g., a family-purpose creditor when the other spouse incurred the obligation) under the labor-mixing statute is to contemporaneously document the bases upon which “reasonable compensation” is determined. Depending upon the amount at issue and the client’s tolerance for the time and expense involved, this may include retaining the services of an independent consultant familiar with the particular industry and the responsibilities and performance of the spouse working in the business.

➤ **Note.** Section 766.63(2) is applicable only for purposes of classifying property under chapter 766. A different rule has developed through case law regarding the appreciation of nondivisible property under chapter 767. For the appreciation in value to be divisible at divorce, there is no requirement that it be “substantial,” that the effort supplied by a spouse be “substantial,” or that reasonable compensation not have been received. *See infra* ch. 11.

For further discussion of section 766.63(2), see section 3.42, *supra*.

## **D. Preserving Management and Control Rights of Marital Property Assets [§ 10.168]**

Management and control of marital property assets is governed by section 766.51. A spouse acting alone may manage and control marital property assets that are held in that spouse's name alone, marital property assets held in the names of both spouses in the "or" form, and marital property assets not held in the name of either spouse. Wis. Stat. § 766.51(1).

A spouse wishing to achieve or preserve exclusive management and control of marital property assets without interference from his or her spouse has several tools available to accomplish this. If assets are held jointly by the spouses in the "or" form, each spouse has the power to change the title or withdraw funds (depending on the type of assets) and retitle the asset in his or her name alone. If the assets are not held by either spouse (i.e., untitled assets), one spouse acting alone has the power to convey the assets into a titled entity held in that spouse's name alone (e.g., a single-member LLC held by that spouse).

The management and control provisions under section 766.51 must be read in conjunction with section 766.70(3), the so-called add-a-name remedy provision, which allows a spouse to petition the court for an order to have his or her name "added to marital property or to a document evidencing ownership of marital property held in the name of the other spouse alone," with certain notable exceptions. The exceptions to the availability of the remedy relate to an interest in various kinds of entities often associated with the operation of a closely held business (e.g., an interest in a partnership or joint venture, membership in an LLC, an interest in a professional corporation or association or similar entity, or stock in a closely held corporation). The exception also applies in the case of an unincorporated business if the other spouse is the only one spouse involved in the operating or managing the business, but it is significant to note that this is the only one of the various exceptions that even mentions an operating business. Thus, for example, it would be possible for a spouse having sole management and control of a brokerage account held in his or her name alone to preclude the availability of a remedy by the nonholding spouse under section 766.70(3) by transferring title of the brokerage account into the name of a single member LLC in which the holding spouse is the sole member.

Another means of sheltering marital property assets from the add-a-name remedy may be through the use of a revocable trust established by the spouse seeking exclusive management and control. Under section 766.51(3), the right to manage and control marital property transferred to a trust is determined by the terms of the trust. Hence, a spouse having sole title to marital property assets could transfer them into a trust of which that spouse is the sole trustee. Although a revocable trust is not listed in the statute as an exception to the add-a-name remedy, the operative language of the statute authorizing the remedy in the first instance specifies its application to “marital property ... held in the name of the other spouse.” Wis. Stat. § 766.70(3). It may be argued that property held in the name of the other spouse *as trustee* is distinguishable from property held directly by the other spouse for purposes of the statute. Whether a court would be so persuaded is uncertain.

For further discussion of the add-a-name remedy, see chapter 8, *supra*.

➤ **Note.** Even if a spouse is successful in maintaining exclusive management and control of marital property assets, he or she continues to owe a duty of good faith to his or her spouse in matters involving such property. See Wis. Stat. § 766.15.

For a discussion of management and control rights generally, see chapter 4, *supra*.

### **E. Limiting Elective Rights at Death [§ 10.169]**

Under chapter 861, the amount of the deferred marital property elective share that may be claimed by a surviving spouse is determined by reference to (1) the value of the “augmented deferred marital property estate” as defined in sections 861.018(1) and 861.02(2), and (2) the extent to which the elective share is deemed satisfied by property retained by or transferred to the surviving spouse under section 861.06. Hence, the important points in limiting the amount recoverable by the surviving spouse as a deferred marital property elective share are (1) to reduce the size of the augmented deferred marital property estate when possible, and (2) to structure interests passing to or for the benefit of the surviving spouse so that they are “counted” toward satisfaction of the elective share.



The most effective way to reduce the size of the augmented deferred marital property estate is to make lifetime transfers of assets that would constitute deferred marital property at death. Hence, for example, if a spouse wants to make a substantial gift to his or her children from nonmarital property assets and he or she owns both individual property assets and predetermination date property assets that would be classified as deferred marital property upon death, the gift should be made from the predetermination date property assets. While the determination of the value of the augmented deferred marital property estate includes a two-year look-back period for gifts of deferred marital property assets, if the donor spouse survives the transfer for two years, the transferred assets are no longer part of the equation.

With regard to having assets considered “property transferred to the surviving spouse” in satisfaction of the deferred marital property elective share, it should be observed that the value of a trust interest created for the survivor is within the definition of *property* used in chapter 861, which incorporates by reference the definition of property under section 851.27. See Wis. Stat. § 851.27 (defining property to include an equitable interest and rights of a beneficiary under a contractual arrangement). Note, however, that a disclaimed transfer in trust is not considered “property transferred to the surviving spouse” for purposes of satisfying the elective share unless the surviving spouse had a general power of appointment over the trust during his or her lifetime or an interest in the trust after the disclaimer. See Wis. Stat. § 861.06(1). Hence, the survivor’s disclaimer of a QTIP marital trust would eliminate consideration of the value of the trust interest in determining the extent to which the elective share has been satisfied.

## **F. Planning Strategies to Maximize Spouse’s Power of Management and Disposition [§ 10.170]**

A spouse who has management and control of a marital property asset has the authority vis-a-vis third parties to “deal with [such] property as if it were property of an unmarried person.” Wis. Stat. § 766.01(11). With respect to his or her spouse, however, a spouse has a duty of good faith in matters involving marital property. Wis. Stat. § 766.15(1). The term *good faith* is not defined in chapter 766. Whether a spouse’s management of marital property assets in a manner that enhances that spouse’s power of disposition over the asset violates the duty of good

faith must be determined on a case-by-case basis. *Id.* Some of the strategies discussed in this section must be considered in that context.

During an ongoing marriage, a spouse can avoid application of the marital property law altogether (at least with respect to assets acquired in the future) by moving from Wisconsin, since chapter 766 applies only “during marriage” as that term is defined. *See* Wis. Stat. §§ 766.01(8), .03(2).

Assuming that both spouses continue to be domiciled in Wisconsin, if one spouse is terminally ill, the other spouse may be able to limit the terminally ill spouse’s power of testamentary disposition over certain marital property assets within the management and control of the non-terminally ill spouse by retitling the assets so that they include a right of survivorship.

➤ **Example.** A husband is incompetent and terminally ill. His will leaves his entire estate to his son, who recently entered treatment for drug addiction. The wife has assets titled in her name alone classified as marital property. She retitles the assets as survivorship marital property. After the husband’s death, the wife places the assets representing the husband’s share of former survivorship marital property into a trust for the benefit of his son.

Another possible way to limit a spouse’s power of testamentary disposition over certain kinds of marital property assets is to cause them to be subject to the terminable interest rule applicable to deferred employment benefits. *See* Wis. Stat. § 766.62(5). Thus, the employee spouse who has the ability to enter into deferred compensation arrangements with his or her employer can cause marital property compensation to fall within the definition of a “deferred employment benefit” under section 766.01(3m) so that his or her spouse’s marital property interest in the asset ceases upon death. *See supra* ch. 4. Whether the deceased spouse’s estate may have a claim against the survivor depends on all of the facts and circumstances.

Forcing the nonholding surviving spouse to affirmatively pursue his or her marital property interest in assets passing at death is another way of potentially limiting the nonholding spouse’s interest. If the holding spouse leaves no estate subject to administration, but rather disposes of all property over which he or she had management and control by nontestamentary means (such as beneficiary designations or transfers by

revocable trust), the surviving spouse has a remedy under section 766.70, but one with a relatively short statute of limitation (one year from date of death, *see* Wis. Stat. § 766.70(6)(b)). If an action is not commenced within that period, the remedy is barred. *See Jackson v. Employee Trust Funds Board*, 230 Wis. 2d 677, 602 N.W.2d 543 (Ct. App. 1999).

Similarly, lifetime gifts of marital property assets to third parties can limit the nonholding spouse's interest in such assets. For a gift made within the amounts specified in section 766.53, the nonholding spouse has no remedy. If the gift exceeds the amount specified in section 766.53, the nonholding spouse has a remedy under section 766.70, but as noted with respect to transfers at death, the burden is on the nonholding spouse to institute an action within a relatively short statute of limitation (for lifetime gifts, within the earliest of one year after notice of the gift, one year after dissolution, or by the deadline for filing claims under section 859.01 after the death of either spouse, Wis. Stat. § 766.70(6)(a)).

Finally, lifetime gifts of property that would be classified as deferred marital property upon death may limit the amount that the survivor can recover by exercising deferred marital property rights under section 861.02.

## **XVI. Asset Protection Planning: Considerations Relating to Creditor Rights [§ 10.171]**

### **A. In General [§ 10.172]**

In some cases, estate planning includes consideration of how to best shield the spouses' assets from creditors' potential claims. Much has been written on the use of "off-shore" trusts for this purpose, and, more recently, "on-shore" trusts in such states as Alaska and Delaware. *See, e.g.,* Allan J. Claypool, "Asset Protection Overview: Techniques in the United States and Offshore," *ACTEC Notes*, Vol. 24, No. 4 (Spring 1999). Discussion of such asset protection planning techniques is beyond the scope of this book. However, for some clients, given the expanded ability of creditors to reach assets under Wisconsin's marital property law, the planner may need to consider planning techniques under the marital property law in an effort to reduce the availability of assets to creditors.

## **B. Creditor Rights Generally Under the Marital Property Law [§ 10.173]**

When only one spouse incurs an obligation but the obligation has been incurred in the interest of the marriage or family, all marital property is available to satisfy the obligation. Wis. Stat. § 766.55(2)(b). Moreover, a family-purpose creditor is not bound by the terms of a marital property agreement classifying as individual property assets that, absent the agreement, would have been classified as marital property, unless the creditor had actual knowledge of the applicable provision of, or was provided with a copy of, the agreement before the obligation was created or incurred. *See* Wis. Stat. § 766.55(4m).

As discussed in section 10.174, *infra*, for clients with potential creditor issues, opting in to marital property classification (by marital property agreement or other available means) can have an adverse impact on the nonincurring spouse. In addition, opting out of marital property classification by means of a marital property agreement can prove ineffective to shield assets from a creditor if the creditor has not been provided with a copy of the agreement in advance or does not have advance actual knowledge of the pertinent provisions of the agreement.

When potential creditor claims are an issue and one spouse has significant individual property assets, careful record keeping to avoid reclassification by mixing under section 766.63 is important. Even if the owning spouse has executed and delivered a unilateral statement under section 766.59 or the spouses have entered into a marital property agreement classifying income from individual property assets as individual property, a creditor without knowledge of the document will not be bound by its terms, even though the document is effective as between the spouses.

## **C. Potential Adverse Impact of Opt-in Marital Property Agreement [§ 10.174]**

Chapter 766 describes the type of property (i.e., marital or nonmarital) that is available to satisfy various types of obligations when only one spouse incurs an obligation (if both spouses incur an obligation—such as by co-signing a note—all property of both spouses, regardless of classification, is available to satisfy the debt except for

property specifically exempt by statute). From a planning standpoint, it is important to recognize that, while opting in to marital property treatment can be helpful in some cases for income tax or estate tax planning purposes, opting in may enhance creditors' recovery rights. See chapters 5, 6 and 7, *supra*, for further discussion.

➤ **Example.** A wife has inherited property from her mother that has appreciated significantly in value since her mother's death. Her husband is in poor health and, while death is not imminent, likely will die within the next several years. The husband's estate is considerably smaller than the wife's (mainly due to a series of bad business deals, some of which are ongoing and for which the husband has executed personal guaranties to a bank). For tax planning purposes, the husband and wife enter into an opt-in marital property agreement, which has the effect of classifying the wife's inherited property as marital property. Later, the bank obtains a judgment against the husband on the guaranties.

While in the above example, entering into an opt-in marital property agreement could provide potential income tax benefits (a stepped-up basis for the wife's inherited assets upon the husband's death) and estate tax benefits (equalized estates for fully utilizing the husband's applicable credit amount and lower estate tax brackets), the adverse creditor situation is the predominant concern. By adopting marital property classification for the wife's inherited assets, the spouses made those assets available to satisfy the judgment against the husband, both during lifetime, *see* Wis. Stat. § 766.55(2), and upon and after the death of either spouse, *see* Wis. Stat. § 859.18.

Hence, the planner should consider each spouse's own outstanding or potential obligations for which marital property ultimately could become available. While many potential tort obligations can be covered adequately by insurance so as to minimize the potential adverse impact of marital property classification, other potential tort obligations, potential commercial obligations, fines, or other liabilities incurred by only one spouse may make opting in to marital property classification inadvisable.

## **D. Reclassification to Limit Amount of Marital Property Assets [§ 10.175]**

Because of the potential adverse impact of creditor claims on marital property, when one spouse has high liability risk, the spouses may wish to avoid classifying assets as marital property or to affirmatively reclassify marital property assets as the individual property of the spouse who is not “high risk” (subject, however, to concerns regarding applicable fraudulent-transfer laws). The manner in which assets are reclassified as individual property may have a significant impact on whether the strategy succeeds. If a marital property agreement is used to classify property that would otherwise have been classified under the law as marital property, the agreement will be effective as between the spouses to cause a reclassification, but a creditor cannot be adversely affected by the agreement unless it has been provided in advance with a copy of the agreement or has advance actual knowledge of the pertinent provisions of the agreement. Wis. Stat. § 766.55(4m).

➤ *Example.* A wife is the owner and insured of a life insurance policy having a cash surrender value of \$50,000. The policy was issued in 1986 following a relocation by the wife and her husband to Wisconsin. As part of their estate planning in 1994, the husband and wife enter into a marital property agreement that provides, among other things, that the life insurance policy insuring the wife’s life is classified as her individual property. In 2009, ABC Bank (which never had knowledge of or received a copy of the marital property agreement) acquires a judgment against the husband on a guaranty he signed with respect to a now-defunct business venture. Thereafter, the bank seeks to execute on its judgment against the cash value of the life insurance policy.

Absent reclassification, the policy would be classified as marital property under section 766.61(3)(a). The reclassification of the life insurance policy as the wife’s individual property by marital property agreement will be effective as between the spouses but ineffective against the bank, since the bank lacked knowledge of the agreement when the husband incurred the guaranty obligation. Assuming the guaranty agreement included a separately signed marital-purpose statement or in fact was entered into in the interest of the marriage or family, the bank may satisfy its judgment against the cash value of the life insurance policy, subject to the limited protection afforded by section

815.18(3)(f) (which provides a limited exemption against execution for life insurance). The bank is entitled to regard the policy as marital property since, in the absence of the marital property agreement, the law would classify the policy as marital property of the spouses.

If the husband and wife had instead reclassified the life insurance policy as her individual property by written consent under section 766.61(3)(e), the bank could not regard the policy as marital property for the purpose of collecting on its judgment. This is because section 766.55(4m) limits the effect of a reclassification with respect to creditors without knowledge only in the case of a reclassification by marital property agreement or decree under section 766.70 (and by cross-reference, a unilateral statement, *see* Wis. Stat. § 766.59(5)). The reclassification by written consent is binding on creditors, even those without knowledge of the written consent (subject, of course, to a creditor's ability to invalidate a transfer under fraudulent-transfer laws, where applicable).

Other ways to reclassify property that, like a written consent, are not subject to the limitation imposed by section 766.55(4m) include reclassification by gift, conveyance (as defined in section 706.01(4)) signed by both spouses, and, in the case of a security, an instrument signed by both spouses that conveys an interest in the security. Each of these methods is an authorized means of reclassifying property under section 766.31(10).

### **E. Potential Benefit of Holding Assets as Survivorship Marital Property or Joint Tenancy Property [§ 10.176]**

Survivorship marital property is not a separate classification but is simply marital property with a right of survivorship upon the death of the first spouse to die. *See supra* ch. 2. During the spouses' joint lifetime, a family-purpose creditor has the ability to reach survivorship marital property assets owned by the spouses. *See* Wis. Stat. § 766.55(2)(b). However, upon the death of a spouse who was the only obligated or incurring spouse with respect to an obligation, a survivorship marital property asset is not available to satisfy the obligation unless the property was secured by a consensual lien or execution on a judgment lien was issued before the spouse's death. Wis. Stat. §§ 766.60(5), 859.18(4)(a).

Holding assets as joint tenancy property gives the same protection from estate claimants, *see* Wis. Stat. § 859.18(4)(a)2., although joint tenancy property has the additional advantage of not being completely available to a family-purpose creditor of one spouse during the spouses' joint lifetime. Hence, if an asset is predetermination date joint tenancy property, preserving that form of ownership may be beneficial to spouses from a creditor protection standpoint both during their joint lifetime and upon the death of the indebted spouse.

Joint bank accounts do not enjoy the same protection from creditors at death as do survivorship marital property assets or joint tenancy assets. Section 859.18(5)(c) provides that a creditor's ability to reach an account under chapter 705 is governed by section 705.07. Section 705.07(2) cross-references chapter 242, which provides creditors with remedies in the case of fraudulent transfers. Section 705.07(2) treats a transfer of an account by reason of death as being fraudulent if the decedent's estate is insolvent under section 242.02 (liabilities in excess of assets). Thus, if marital property assets or nonmarital property assets pass to a surviving spouse by reason of the death of an indebted spouse, and the assets of the decedent's estate are insufficient to pay the creditor's claim, the creditor may pursue a fraudulent transfer remedy under chapter 242.

Hence, seemingly insignificant differences in the manner in which assets are held during lifetime can lead to strikingly different results upon the death of one spouse.

➤ **Example.** A husband is the only incurring spouse with respect to a family-purpose obligation that results in a creditor obtaining a substantial judgment against him. Before the creditor has an opportunity to execute on the judgment, the husband dies leaving no assets subject to administration. At death, the only significant assets in which he has an interest are (1) a joint savings account with his wife at ABC Bank and (2) a money-market mutual fund with XYZ Mutual Fund Company held in the names of the husband and wife as "joint tenants," which was established by the husband and wife after their determination date.

In this example, because the husband's estate is insolvent, under sections 859.18(5)(c) and 705.07(2) the creditor may pursue a fraudulent transfer remedy under chapter 242 against the wife with respect to the joint bank account. The money-market mutual fund, however, is survivorship marital property under section 766.60(4)(b)1.a. The wife



therefore succeeds to ownership of the mutual-fund account free of any claim by the creditor. Wis. Stat. §§ 766.60(5), 859.18(4)(a)1.

Assets passing by will substitute agreement do not enjoy the same exemption from creditor claims as survivorship marital property assets. *See* Wis. Stat. § 859.18(6). *See also* Wis. Stat. § 705.10(2) (use of nonprobate transfer at death under section 705.10 does not limit rights of creditors under other laws).

## **F. Terminating Applicability of Chapter 766 by Change of Domicile [§ 10.177]**

For clients planning in a hostile creditor environment (e.g., when a creditor has already obtained a judgment and is pursuing collection), avoiding the ongoing accumulation of marital property assets may require a change of domicile by at least one spouse.

➤ **Example.** A husband and wife are domiciled in Wisconsin. The wife makes a substantial income from her business as a sales representative for a pharmaceutical company. The husband has recently become a judgment debtor as a result of a failed business venture. The creditor garnishes the wife's wages. The spouses never entered into a marital property agreement of which the judgment creditor had knowledge or receipt.

Under the example, reclassifying the wife's employment earnings as individual property by marital property agreement would be ineffective to prevent the creditor from garnishing her wages, since the creditor would not have had knowledge of the agreement when the obligation was incurred. However, if either the husband or wife or both cease to be domiciled in Wisconsin, the marital property law will cease to apply. *See* Wis. Stat. §§ 766.03(2), .01(8). While the cessation of domicile in Wisconsin will not prevent the creditor from reaching previously accumulated marital property assets, *see* Wis. Stat. § 766.03(3), the wife's future earnings will not be marital property reachable by husband's judgment creditor.

## **XVII. Selected Forms [§ 10.178]**

### **A. In General [§ 10.179]**

The forms used in estate planning in a community property jurisdiction are generally the same as those used in common law jurisdictions. Nevertheless, estate planning differs significantly under the two systems because the ownership of assets by spouses is much different. Occasionally under a community property system, some forms based on common law concepts will need to be modified to account for marital property. The forms in this part of the book will primarily be the ones that must be modified.

For other forms of wills and trusts with an emphasis on marital property, see *Eckhardt's Workbook for Wisconsin Estate Planners, supra* § 10.1.

### **B. Revocable Trust Created by Both Spouses for Marital and Nonmarital Property [§ 10.180]**

One of the forms that must be modified in Wisconsin is the revocable trust form designed to hold marital property. If marital property is transferred to a revocable trust, both spouses will be grantors for tax purposes. The spouses may or may not be co-settlors for purposes of section 701.01(5).

The following form assumes that the spouses join in the creation of the trust. Both are settlors. It also assumes that nonmarital property may also be transferred to the trust.

This book is not a general forms book. The purpose of this form is to illustrate some of the matters that must be considered when a revocable trust for marital property is prepared.

(husband and wife)

#### **REVOCABLE TRUST AGREEMENT**

This is a trust agreement between (husband and wife), the Settlers, and (trustee's name), the Trustee. The trust created by this agreement

may be referred to as the (husband and wife's surname) REVOCABLE TRUST.

➤ **Comment.** The husband and wife are both settlors. Section 766.31(5) provides that the transfer of property to a trust does not by itself reclassify the property. One spouse may have exclusive management and control of marital property under section 766.51(1)(am). If so, that spouse may fund the revocable trust alone, in the exercise of his or her management powers. After the assets are transferred to the trust, section 766.51(3) provides that the right to manage and control the marital property is determined by the terms of the trust. However, the assets remain marital property after the transfer to the trust under section 766.31(5). *See supra* ch. 2. The Comment to UMPA § 4 states that “a trust created by one spouse would necessarily be measured by the good faith provisions of [section 766.15].” If the trust is created by one spouse alone, and the other spouse does not want the property in the trust, the other spouse may pursue a remedy provided under section 766.70. For a discussion of remedies, see chapter 8, *supra*.

## **I. Administration During Our Lifetimes**

**A. Initial Principal and Additions.** We hereby deliver to the trustee as the initial principal of the trust the property described in the attached Schedules A and B. Marital property is described on Schedule A and nonmarital property is described on Schedule B. Each settlor's ownership interest is indicated on Schedule B. We may transfer additional property or rights to receive property to the trustee from time to time, and the trustee will accept the same.

Marital property assets transferred to the trust by us (or either of us), as it may be invested and reinvested from time to time, together with the income from such marital property, shall retain its character as marital property under section 766.31(5) of the Wisconsin Statutes, subject, however, to the terms of this agreement.

Assets of either settlor that are other than marital property (*nonmarital property*), as it may be invested and reinvested from time to time, shall retain their character as the property of the settlor who transferred such property to the trustee, subject, however, to the terms of this agreement. The income of nonmarital property assets transferred to this trust shall be marital property under section 766.31(4) of the Wisconsin Statutes, unless classified as individual property by a marital property agreement

or unilateral statement classifying income from nonmarital property as individual property.

If marital property assets such as life insurance proceeds or retirement benefits are payable to the trustee of this trust after the death of one of us, nothing in this agreement shall be construed as in any way limiting the rights of either of us.

➤ **Comment.** The form contemplates that marital and nonmarital property will be transferred to the trust. This will impose additional record keeping responsibilities on the trustee.

I.R.C. § 1014(b)(6) provides that both halves of community property receive a full adjustment in basis on the death of one spouse. This form assumes that the spouses want I.R.C. § 1014(b)(6) to apply. See chapter 9, *supra*, for a discussion of I.R.C. § 1014(b)(6) as it applies to assets in a trust.

The final paragraph in the part of the form above is intended to apply to nonprobate assets that are made payable to the trustee. Since these assets may not be transferred to the trust during the marriage, the language in the form providing that marital property retains its character may not apply. The proceeds will be received by the trustee after the death of a spouse and, since the marriage will have terminated, will no longer be marital property. Generally, if the decedent spouse with management powers makes a nonprobate disposition of the surviving spouse's marital property interest, the surviving spouse has a remedy. *See supra* ch. 8, *infra* ch. 12.

**B. Income and Principal of Marital Property.** Any net income of this trust from marital property during our joint lifetimes shall be distributed to or applied for the benefit of us or either of us at least quarterly as marital property. During our joint lifetimes, the trustee may distribute to or for the benefit of us or either of us such amounts of principal of the marital property as the trustee in its discretion shall consider advisable for expenses of maintenance, support, medical care, comfort, or other benefit.

**C. Income and Principal of Nonmarital Property.** Any net income this trust may have from nonmarital property shall be paid to or applied for the benefit of the settlor who contributed the property to the trust except that if the trustee considers it in that settlor's best interests, it may, in its discretion, apply that income for the benefit of the other settlor. The trustee may distribute to either settlor such amounts of principal of nonmarital property as the trustee in its discretion shall

consider advisable for expenses of maintenance, support, medical care, comfort, or other benefit.

➤ **Comment.** Parts B and C above do not authorize distributions to children of the settlors. Since each spouse can withdraw marital property, the spouses themselves can discharge any legal obligations they owe for the support of children. If the trustee could distribute marital property to adult children, this might be contrary to the gift limitation of section 766.53, and it is arguable that the character of the marital property would not be preserved because the trustee could make gifts of marital property that a spouse might not make.

**D. Revocability, Withdrawals, Additions.** While both of us are alive, either of us may:

1. Withdraw all or part of the income from marital property assets or nonmarital property assets (if the income of such nonmarital assets is classified as marital property) and all or any part of the marital property in this trust upon giving reasonable notice in writing to the trustee and the other settlor. Any such withdrawals shall be delivered to the settlors as marital property.

2. Withdraw property derived from the nonmarital property that he or she may have contributed (including the income therefrom if such income is classified as individual property of such settlor) upon giving reasonable notice in writing to the trustee.

While both of us are alive, both of us, acting together, may amend or revoke this trust in whole or in part at any time and from time to time by a signed written instrument. An amendment or revocation shall become effective when signed, but the trustee shall not be liable for any action taken under the terms of the trust as they existed before the trustee received the amendment or revocation. Following any complete revocation, the trustee shall distribute to us as marital property all marital property remaining in the trust and shall distribute all nonmarital property remaining in the trust to the settlor who contributed it. Marital property assets contributed by a settlor with sole management and control of such marital property assets shall be distributed to that settlor.

➤ **Comment.** The part above requires both spouses to join in an amendment of the trust. This power must be carefully considered. If one spouse becomes incompetent, that spouse cannot join in the amendment. However, it appears that the guardian of the spouse may join under section 54.20(2)(h) with court approval. The

considerations concerning joinder for an amendment are similar to the considerations necessary in deciding whether to use a will substitute agreement.

Subparagraph D.2. requires that withdrawals of marital property be distributed to both spouses as marital property, except in the case of marital property assets contributed to the trust by a settlor who had sole management and control of a marital property asset; in that case, the asset would be distributed to the contributing settlor (but would retain its character as marital property).

## **II. Administration After Death of a Settlor**

All property that is or becomes subject to the terms of this trust instrument at the time of or after the death of a settlor shall be paid or distributed as follows:

### **A. Payment of Claims, Expenses, and Taxes**

1. If a settlor dies and a personal representative is appointed for the deceased settlor's estate, this trust shall be indebted to the personal representative for any amount the personal representative may demand in a writing stating that the demand is made for the purpose of paying claims, funeral expenses, expenses of administration, pecuniary legacies, family allowances by court order, or taxes of any kind. Upon receipt of such a demand this trust shall terminate in favor of the deceased settlor's estate as to an amount equal to the amount demanded and the trustee shall distribute such amount to the personal representative. In any event, the trustee may pay to the deceased settlor's estate such amounts as the trustee determines, in its absolute discretion, will benefit the beneficiaries of this trust.

2. If a settlor dies and a personal representative is not appointed for the deceased settlor's estate, the trustee shall pay all gifts and bequests of cash and specific property in the document or documents that are the deceased settlor's last will admitted to probate, the deceased settlor's funeral expenses, and those expenses of administration and death taxes (estate, inheritance and like taxes, including any interest and penalties but not including any generation-skipping transfer taxes) that are payable as a result of the deceased settlor's death. Notwithstanding the above, the trustee shall not pay, or if required to pay, shall seek reimbursement for, the amount of the increase in expenses of administration and death taxes resulting from the inclusion in the deceased settlor's estate for such tax purposes of an unexercised power of appointment, property in which the deceased settlor had a qualifying income interest for life under I.R.C. § 2056(b)(7) or § 2523(f), and transfers, whether during the

settlor's life or as a result of the settlor's death, to or for anyone who is not a beneficiary of the deceased settlor's last will or any trust established by the deceased settlor.

**3.** All payments in 1. or 2. above, except interest, shall be charged against that portion of the principal of this trust includible in the deceased settlor's estate for federal estate tax purposes and any interest so paid shall be charged to the income thereof, except as follows:

**a.** Any such payment of taxes and last illness and funeral expenses arising on the death of the first settlor to die shall be charged against the principal of the family trust created by the death of that settlor and any interest shall be charged to the income of the family trust.

**b.** Any such payments for legally enforceable claims that represent obligations for which all former marital property is obligated shall be charged to the trust estate before the division specified in subparagraph II(B); except that nonmarital property or the proceeds thereof contributed by the surviving settlor shall not be subject to such obligations. Any such payments shall be charged to the decedent's interest in nonmarital property, the decedent's interest in marital property, and the surviving settlor's interest in marital property, in that order.

**c.** Any such payments for legally enforceable claims that represent obligations for which the deceased was obligated at death that were not incurred in the interest of the marriage or the family shall be charged to the deceased settlor's interest in the principal of the trust estate and not to the surviving settlor's interest before the division specified in subparagraph II(B).

**4.** In no event shall the trustee make any payment referred to in subparagraph II.A. from: (a) property added to this trust by anyone other than us or our estates; (b) property transferred to this trust by the exercise by either of us of any power of appointment other than a general power of appointment, or (c) any property, such as life insurance proceeds, that would otherwise be immune from the claims of creditors and if such payment would cause that property to be subject to the claims of creditors; provided, however, that such proceeds and other property may be used for the purchase of assets from a deceased settlor's estate at fair market value.

**5.** Notwithstanding any provision of this instrument, no portion of any payments made under subparagraph II.A. (or such payments made by an estate) shall be allocable or chargeable against any distribution from this trust with respect to which a federal estate tax marital deduction is

claimed, unless and only to the extent that the other assets available for such payments are insufficient.

➤ **Comment.** Subparagraph II.A authorizes the trustee to pay claims, expenses, and taxes on the death of either settlor. Some commentators caution against including authority to remit assets for the payment of claims on the basis that this may unnecessarily expose to claims of estate creditors assets that otherwise may not be reachable. The tax payment clause is a sample only and should be modified to fit the particular clients' situation.

On the death of the first spouse to die, taxes and expenses are charged to the family trust, which always consists of the deceased spouse's one-half interest in marital property and the deceased spouse's nonmarital property, less any marital deduction amount.

On the death of the surviving spouse, taxes and expenses are charged to the survivor's trust because that is the principal includible in the "deceased settlor's" estate for tax purposes.

The payment of claims after one spouse dies can be an extraordinarily complicated matter. In the form, the family trust bears the burden of the claims because it receives the balance of the trust estate after the survivor's trust is funded. The survivor's trust receives the surviving spouse's interest in marital and nonmarital property. The form does not specify whether the family trust has a right of reimbursement from the survivor's trust.

**B. Division Into Trusts.** Upon the death of the first of us to die (*deceased spouse*), the trustee shall divide the assets remaining in or passing to this trust into two separate trusts, hereinafter called the survivor's trust and the family trust, as follows:

1. The survivor's trust shall consist of: (a) the interest of the settlor who survives the deceased spouse (*surviving spouse*) in marital property; (b) the surviving spouse's nonmarital property, if any; and (c) the smallest amount of the remaining property available for distribution under subparagraph II.B.1. necessary to eliminate (or, if that is not possible, to minimize) the net federal estate tax payable by the deceased spouse's estate or this trust. The term *net federal estate tax* means the estate tax imposed by I.R.C. § 2001 as a result of the first spouse's death reduced by (i) the then applicable credit amount and (ii) the then available credit for state death taxes paid to the extent that a state death tax computed on the basis of or with reference to that credit is not thereby caused or increased. In determining the amount distributable under subparagraph II.B.1.c., the trustee shall use the final federal estate



tax values in the deceased spouse's estate and shall consider all factors that affect the computation of the distributable amount, such as property passing outside the terms of this subparagraph II.B.1. that does not qualify for the federal estate tax marital deduction, and charges to principal that are not deducted in computing the federal estate tax. Each asset distributed in satisfaction of the amount under subparagraph II.B.1.c. shall be valued at its value on the date it is distributed. We both recognize that the amount passing under subparagraph II.B.1.c. may be affected by the actions of the fiduciaries in exercising certain tax elections. We also recognize that it is possible, depending upon the size of the estate, the year of death, and other factors, that no amount will pass under subparagraph II.B.1.c.

**2. The remaining property shall be distributed to the family trust.**

➤ *Comment.* After claims, expenses, and taxes are paid, the trust document must identify the beneficiaries and must describe their beneficial interests. Of course there are many possibilities, depending on the spouses' wishes. If a certain spouse dies first, the spouses may want the entire trust to terminate and all assets to be distributed to the surviving spouse, or the trust to continue as one trust for the benefit of the surviving spouse, or the trust assets to be divided into two separate shares, each share consisting of each spouse's interest in marital property and nonmarital property.

If the trust estate will be divided, the spouses must consider how each share will be distributed. The decedent's share may be distributed outright to persons other than the surviving spouse, for example, children. The survivor's share may stay in trust for the survivor's lifetime, subject to a power to revoke, with dispositive provisions. The decedent's share may stay in an irrevocable trust for the benefit of the surviving spouse, with dispositive provisions at the survivor's death that minimize federal estate tax on the surviving spouse's death. These are just a few of the possibilities.

These considerations upon the death of the first spouse are not unique to estate planning in Wisconsin. For example, a typical estate plan in Wisconsin when the value of the spouses' combined assets exceeds the applicable exclusion amount calls for a division of assets while both spouses are alive so that each spouse owns assets. Each spouse may solely own assets or the spouses may own assets together as tenants in common. When each spouse owns assets in a common law property jurisdiction, the disposition of each spouse's property must be considered.

The form in this section is intended to be used when all the following factors are present:

1. The spouses own property having a combined value that exceeds the federal exemption equivalent (applicable exclusion amount) discussed in chapter 9, *supra*.
2. One spouse or both spouses own nonmarital property.
3. The spouses wish to avoid federal estate tax on the predeceasing spouse's death and minimize federal estate tax on the surviving spouse's death.

➤ **Note.** This form does not purport to address the differences between the federal estate tax system and the Wisconsin estate tax system. Hence, depending upon the size of the first deceased settlor's estate for estate tax purposes, there could be Wisconsin estate tax due but no federal estate tax due. After 2004 (at least until the sunset of the federal tax changes in made in 2001) there no longer will be an "applicable credit amount" for federal estate tax purposes.

➤ **Note.** The form assumes the existence of a federal estate tax system at the death of the first spouse. Hence, the so-called *repeal year* (2010) under the federal tax law changes made in 2001 has been disregarded.

The form calls for a division of the trust assets into two trusts upon the first death: a survivor's trust, and a family trust. The survivor's trust consists of the survivor's interest in marital property and nonmarital property. The family trust consists of the remaining trust assets (decedent's interest in marital property and nonmarital property less claims, taxes, and expenses), with one exception. The form contains a *formula pecuniary marital clause* directing the trustee to distribute from the predeceasing spouse's interest to the survivor's trust whatever is necessary to eliminate federal estate tax (*as noted above, this will not necessarily eliminate Wisconsin estate tax*).

In addition to the assets held by the trustee at the first death, assets such as probate assets poured over from the will, life insurance, and retirement benefits may be transferred to the trustee after death.

**C. Savings Clause.** It is intended to qualify the distribution under subparagraph II.B.1.c. for the federal estate tax marital deduction, and this instrument is to be construed accordingly. Notwithstanding any provision in this instrument to the contrary, the trustee shall have no discretion or power, the existence or exercise of which would disqualify

such distribution for the marital deduction. Any power to invest in or retain unproductive property in the survivor's trust shall be subject to the power in the surviving spouse to require that any such property be converted into productive property within a reasonable time following such spouse's written request.

➤ *Comment.* Subparagraph C is a standard savings clause.

### III. Survivor's Trust

All property that is part of this survivor's trust shall be held and administered as a separate trust as follows:

**A. Income.** The net income beginning as of the date of the deceased spouse's death shall be paid to or for the benefit of the surviving spouse, not less frequently than quarterly as long as he or she lives.

**B. Invasion of Principal.** It is our desire that, if the assets are sufficient, the surviving spouse be amply provided for so as to be able to maintain the approximate standard of living maintained during our lifetimes. Accordingly, the trustee is authorized in its discretion to distribute to the surviving spouse or apply for his or her benefit such amounts of principal as the trustee shall consider desirable for the surviving spouse's comfortable support, maintenance, general welfare, and any other worthwhile purpose, taking into account other resources known to the trustee to be available.

**C. Right to Withdraw Principal.** The trustee shall distribute to the surviving spouse during his or her lifetime such part or all of the principal of this trust as he or she from time to time requests in writing.

➤ *Comment.* Subparagraph III.C gives the surviving spouse the power to withdraw all the assets in the survivor's trust. This power may be necessary to obtain the full adjustment in basis for marital property held in the trust. Rev. Rul. 66-283, 1966-2 C.B. 297. The survivor's trust may also include property of the decedent due to the pecuniary formula clause. A power to withdraw is not necessary for this property. It can be distributed to a separate trust for the surviving spouse as long as it qualifies for the marital deduction.

**D. Distribution on Surviving Spouse's Death.** The surviving spouse shall have the power to appoint by will the principal and any income accrued and undistributed at the time of death to such person or

persons and upon such terms and conditions, whether outright, in trust, or otherwise, as he or she may choose, by specific reference to this power of appointment in his or her will. This power shall be unrestricted and shall include the power to appoint to his or her estate. To the extent that he or she shall fail to effectively exercise this power, then the undistributed principal and accrued income shall be added to the family trust.

➤ **Comment.** Paragraph III is a “power of appointment” trust. Since a portion of the decedent’s property may pass to the Survivor’s Trust, the entire trust must qualify for the marital deduction. The general power of appointment complies with I.R.C. § 2056(b)(5).

#### **IV. Family Trust**

All property that is part of this family trust shall be held and administered as a separate trust as follows:

**A. Income and Principal.** The net income of this trust shall be distributed to or applied for the benefit of the surviving spouse, not less frequently than quarterly for his or her lifetime. In addition, the trustee may distribute to or apply for the benefit of the surviving spouse such amounts of the principal of this trust as the trustee in its absolute discretion, shall determine. Following the surviving spouse’s death, the current and accumulated net income and the principal of this trust may be distributed to or applied for the benefit of any one or more of the group consisting of our children, and our children’s issue, in such amounts and at such times as the trustee, in its absolute discretion, may determine. The terms *children* and *issue* mean children and issue of the predeceasing spouse who also are children and issue of the surviving spouse.

➤ **Comment.** It is intended that the term *our children* refers to the children common to both settlors. If the surviving spouse may remarry and have more children, and it is intended that they be included, the form must be modified.

#### **B. Guides to Trustee**

1. The trustee shall have no duty to preserve principal intact to the extent it shall consider its current use in the best interests of the current beneficiaries. Distributions may be made for a beneficiary’s care, comfort, maintenance, education (including graduate or technical education), purchases of homes, purchases of businesses, or any other

worthwhile purpose. The trustee shall have no liability to any beneficiary for any good-faith exercise of its powers to make or withhold distributions of principal. It is suggested that no principal be distributed to or for the surviving spouse until the survivor's trust assets have been exhausted, but this suggestion is not mandatory.

2. Whenever discretion is given to make distributions among a group of beneficiaries, the distributions shall be made on the basis of the purposes of this trust and the needs and circumstances of the beneficiaries. It is anticipated that the needs of beneficiaries may not be equal and that distributions to them may also be unequal. However, the trustee may charge all or any part of any distribution hereunder against the share of any beneficiary (or his or her successors in interest) if it shall consider this most equitable under the circumstances. The trustee may consider other resources known to it to be available to beneficiaries.

**C. Division into Shares.** At such time after the death of the survivor of us, when there is no living child of ours under the age of twenty-two (22) years, the then remaining net assets of this trust shall be divided into equal shares so that there is one share for each of our then living children and one share for each of our then deceased children who is survived by then living issue.

1. Each share for a then living child shall be distributed to that child.

2. Each share for a then deceased child who is survived by then living issue shall be paid to or held for the benefit of such one or more of the group consisting of my child's issue as my child may have appointed (whether outright, in trust or otherwise) by specific reference to this power in his or her will. Any portion of the then deceased child's share not so appointed shall be distributed to my child's then living issue by right of representation.

**D. Distributions for Beneficiaries.** Distributions of principal or income to or for the benefit of any person who is less than twenty-two (22) years of age or is, in the sole judgment of the trustee, incompetent to manage such property may be made in the trustee's sole discretion in any one or more of the following ways, and the trustee shall not be responsible for the application of such distributions:

1. Distribution to the person even if he or she has not reached the age of majority;

2. Distribution for expenses of support, health, education, comfort or welfare of the person;

3. Distribution to the legal guardian of the person or to a custodian for the person under any applicable Uniform Gifts to Minors Act; or

4. Retention in a separate trust for the person until, in the trustee's discretion, payment may be made by any of the methods set out above. The income and principal of the separate trust may be distributed to or for the benefit of the person at such times and in such amounts as the trustee, in its absolute discretion, may determine. The assets remaining in the separate trust at the time of the person's death shall be distributed to his or her estate.

**E. Failure of Beneficiaries.** If at any time after the survivor's death there shall be any assets of any trust established under this agreement not otherwise disposed of, those assets shall be divided into two equal shares to be distributed as follows: One such share shall be distributed to such then living persons and in the proportions that property of the first spouse would have been distributed if he or she had died unmarried and intestate immediately after this paragraph became operative, and the other share shall be distributed to such then living persons and in the proportions that the surviving spouse's property would have been distributed if the surviving spouse had died unmarried and intestate immediately after this paragraph became operative, provided, however, that the intestate succession laws of the state of Wisconsin in effect at the time of execution of this instrument shall determine the distributions under this paragraph.

## **V. Powers and Duties**

*(Insert desired powers)*

➤ **Comment.** This form assumes that an independent, corporate fiduciary is the trustee. Special considerations must be taken into account if the surviving spouse or a trust beneficiary is the trustee.

## **VI. Trustee and Successor**

*(Insert name of trustee, provisions with respect to resignation and removal, and similar provisions)*

## **VII. Accounts**

*(Insert provisions with respect to trustee's duty to account)*

### VIII. Miscellaneous Provisions

*(Insert miscellaneous provisions such as definitions, change of situs, and rules for interpretation of the document)*

Dated: \_\_\_\_\_

WITNESSES:

_____	_____
	<i>(name of spouse)</i>
_____	
_____	_____
	<i>(name of spouse)</i>
_____	

*(Name of trustee)* accepts the foregoing, consents to act as trustee under the terms of the foregoing trust instrument, and acknowledges receipt of the property referred to in paragraph I.

*(Name of trustee)*  
By: \_\_\_\_\_  
Its: \_\_\_\_\_  
By: \_\_\_\_\_  
Its: \_\_\_\_\_

### C. Forced Election Clause for Will [§ 10.181]

It is my intention by this will to dispose of my individual property, my predetermination date property, whether or not it is deferred marital property, and all marital property that I own together with my spouse. I believe that my spouse will benefit by taking under the provisions of this will made for *(him)* *(her)* and I request that *(he)* *(she)* accept these provisions rather than claim the rights in such property passing under this will that *(he)* *(she)* has. If my spouse elects, however, to retain *(his)* *(her)* interest in marital property, to make the deferred marital property election in chapter 861 of the Wisconsin Statutes, I then direct that the bequest in *(his)* *(her)* favor of the residence, household goods and

personal effects contained in Paragraph \_\_\_ of this will shall be valid and operative and that all other bequests, devises, and provisions in this will in *(his) (her)* favor are void and have no effect; but the remaining provisions herein in favor of other persons shall nevertheless be valid and operative in the same manner as though my spouse predeceased me.

➤ **Comment.** This form can be used to put the surviving spouse to a forced election. This is not the same as the equitable election in section 853.15. The consequences of an equitable election are spelled out in section 853.15. The consequences of a forced election are spelled out in the instrument.

The forced election clause above contains a forfeiture provision if the surviving spouse elects to retain his or her interest in marital property or makes the deferred marital property election in chapter 861. The form is drafted so that doing either invokes the forfeiture. Of course, the form could be drafted in a number of other ways. For example, the form applies to both marital property and deferred marital property, but could be tailored to apply to one or the other.

➤ **Caution.** The tax consequences of a forced election are uncertain. Therefore, this form should be used with caution. *See supra* ch. 9.

#### **D. Voluntary Election Clause for Will [§ 10.182]**

It is my desire by this will to dispose of my individual property, my predetermination date property, and all marital property that I own together with my spouse. I believe that my spouse will benefit by taking under the provisions herein made for *(him) (her)*. I request that *(he) (she)* accept these provisions rather than claim any rights that *(he) (she)* has in property passing under this instrument. If my spouse elects to take the rights given *(him) (her)* by law, *(he) (she)* shall nevertheless be entitled to all benefits given *(him) (her)* by this will with respect to all property remaining subject to it. If my spouse elects to take the rights given *(him) (her)* under law, I confirm *(his) (her)* interest in all marital property and hereby state my intention that this will dispose only of my interest in property.

➤ **Comment.** This clause is used when the decedent suggests a disposition of the surviving spouse's interest in marital property. However, the suggestion does not put the spouse to an election.



The tax consequences of a voluntary election are far more certain than the tax consequences of a forced election. *See supra* ch. 9.

### **E. Intent with Respect to Equitable Election: No Election [§ 10.183]**

I hereby declare that my spouse owns a one-half interest in marital property, if any, and that I intend that this will dispose only of my interest in such property. I do not intend to transfer my spouse's interest in our marital property.

➤ **Comment.** The 1985 Trailer Bill amended the equitable election statute, section 853.15, to enable the maker of a will to indicate in the will whether or not the maker intends to put the surviving spouse to an equitable election.

This form states that it is the maker's intent to not transfer the surviving spouse's interest in marital property. The next form states the maker's intention to put the spouse to an equitable election.

### **F. Intent To Put Surviving Spouse to Equitable Election [§ 10.184]**

It is my intent by this will to dispose of my spouse's interest in marital property. It is my intent that my spouse elect, under section 853.15 of the Wisconsin Statutes, between accepting the benefits of this will and transferring (*his*) (*her*) marital property interest, if any, in accordance with this will; and retaining (*his*) (*her*) marital property interests interest, if any, and not taking under this will. If my spouse elects not to take under this will, the property given (*him*) (*her*) under this will shall be assigned to (*name of person to receive surviving spouse's property*).

➤ **Comment.** This form is designed to put the surviving spouse to an equitable election under section 853.15. Section 853.15 permits the will to state whether there is an election and, if so, what the consequences of the election are.

Specifying the consequences will depend on the exact circumstances. The form in this section simply restates the consequences that are specified by section 853.15 if the will is silent on the matter.

## **G. Apportionment of Expenses of Administration**

### **[§ 10.185]**

My personal representative may pay expenses of administration of my estate out of my interests in marital property, nonmarital property, or both, as my personal representative, in its sole discretion, may determine is in the best interests of my estate.

➤ **Comment.** Section 857.04(1) provides that the personal representative shall pay expenses of administration out of the decedent's interests in marital property and in property other than marital property on a prorated basis according to the value of those interests. Depending on the circumstances, such a proration may not be desirable. For example, if section 857.04(1) is applied literally, property may have to be sold to pay expenses of administration. In this form, the maker of the will gives the personal representative discretion to pay all expenses of administration from residue without charging the expenses to any particular assets. Presumably, the maker of a will can alter the effect of section 857.04(1), although it is not expressly permitted by the statute.

## **H. Declaration of Gift to Spouse Reclassifying Marital Property to Individual Property [§ 10.186]**

### **DECLARATION OF GIFT**

I, (name of donor) of the city of (city), county of (county), state of Wisconsin, own a marital property interest in the following shares of stock of (name of company).

*(describe certificates)*

I desire to give the above described property to my spouse, (name), as *(his)* *(her)* individual property.

To carry out my intention to make this gift, I do hereby give and deliver the above described property to (name of spouse) to be *(his)* *(hers)* absolutely.

It is my purpose and intention to vest all incidents of absolute ownership of the above described property in my spouse from this time forward, including all income attributable to such property after this gift.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
Donor

#### ACCEPTANCE

I accept delivery of and dominion over the above gift.

Dated \_\_\_\_\_

\_\_\_\_\_  
Donee

➤ **Comment.** Section 766.31(10) permits spouses to reclassify property by gift. However, the Act does not define *gift*. The traditional common law definition of gift requires four elements: intent; dominion by the donor; delivery; and dominion by the donee. Under the former common law property system, as a practical matter, gifts between spouses were implemented by simply changing the title document, if there was one, or by delivery of possession if there was no title document. Whether the former methods used to implement gifts suffice under the Act is not certain. Under the Act, changing title may reflect a change of management rather than ownership.

The purpose of this form is to provide evidence that a gift has occurred. Of course, mere execution of the form is not enough. There must be a gift in fact between the spouses.

The above form expressly states that the income of the donated asset is the individual property of the donee spouse, which is consistent with section 766.31(10) as it relates to gifts between spouses.

# I. Unilateral Statement Classifying Income Attributable to Nonmarital Property as Individual Property [§ 10.187]

## UNILATERAL STATEMENT CLASSIFYING INCOME ATTRIBUTABLE TO NONMARITAL PROPERTY AS INDIVIDUAL PROPERTY

Pursuant to section 766.59 of the Wisconsin Statutes, the undersigned spouse classifies the income attributable *(to all of his or her property other than marital property, whether now or hereafter acquired) (to the following described property . . . and property acquired in exchange for or with the proceeds of that property)* as individual property. This statement is effective on the later of (date) the date this statement is executed, or the date of marriage.

Dated: \_\_\_\_\_

\_\_\_\_\_  
Signature

STATE OF WISCONSIN  
COUNTY OF \_\_\_\_\_

This instrument was acknowledged before me on (date) by  
(name).

\_\_\_\_\_  
Notary Public, State of Wisconsin  
My commission expires \_\_\_\_\_

### ACKNOWLEDGMENT

I acknowledge receipt of a copy of the foregoing statement.

Dated: \_\_\_\_\_

\_\_\_\_\_  
Signature

➤ **Comment.** This form is designed to accomplish a so-called *unilateral statement* under section 766.59. For a discussion of the statute, see sections 10.164–.167, *supra*. The receipt has been

included to avoid the need for service by certified mail. The form may be used by an existing spouse or a prospective spouse.

**J. Written Consent to Reclassify Life Insurance Policy  
as Individual Property of the Other Spouse  
[§ 10.188]**

WRITTEN CONSENT TO LIFE INSURANCE BENEFICIARY  
DESIGNATION

I, (name), do hereby consent to the designation by my spouse, (name) as the beneficiary of the proceeds of Policy # \_\_\_\_\_ which insures my spouse, (name).

This written consent is effective to reclassify all of my interest, if any, in the ownership interest and proceeds of said life insurance policy as the individual property of my spouse.

In view of the fact that this written consent is effective to reclassify my interest in the ownership interest and proceeds of said life insurance policy as the individual property of my spouse, I understand that this written consent is effective to limit my rights in the policy.

This written consent is *(revocable)* *(irrevocable)*. This consent is effective only with respect to the beneficiary named in this instrument.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
Witness

\_\_\_\_\_  
Signature of Consenting Spouse

➤ **Comment.** The statutes provides for two types of written consents: a written consent by creditors under section 766.55(4) and a written consent concerning life insurance insuring a spouse under section 766.61(3)(e).

A spouse may consent to the designation of another person as the beneficiary of the proceeds or consent to the use of property to pay premiums on life insurance. Wis. Stat. § 766.61(3)(e). This form is only a consent to the designation of a beneficiary. The form in

section 10.186, *infra*, is a consent to the use of property to pay premiums.

A written consent is effective only with respect to the beneficiary named in it unless the written consent provides otherwise. Wis. Stat. § 766.61(3)(e). This form pertains to a specific beneficiary.

The extent to which the written consent relinquishes or reclassifies the consenting spouse's marital property interest depends on the terms of the written consent. Wis. Stat. § 766.61(3)(e). In general, there are two choices. First, the consenting spouse can relinquish his or her marital property interest in the policy or the proceeds in favor of the beneficiary. Such a consent may be a gift to the beneficiary subject to gift tax. *See supra* ch. 9. Second, the consenting spouse can reclassify his or her marital property interest as the individual property of the other spouse. Such a reclassification may also be a gift. However, if it is, it should qualify for the federal gift tax marital deduction. *Id.* Since a gift to the spouse is likely to be tax free, the form in this section results in a gift to the other spouse, rather than to the beneficiary.

A written consent is revocable unless it expressly provides otherwise. Wis. Stat. § 766.61(3)(e). This form provides a choice. If the consent is irrevocable, the consenting spouse should be made aware of the property rights relinquished. See chapter 14, *infra*, for a discussion of joint representation.

Section 766.61(3)(e) provides that the revocation of a written consent is effective no earlier than the date on which it is signed by the revoking spouse; section 766.61(3)(e) does not operate to reclassify any property that was reclassified by the written consent or in which the revoking spouse relinquished an interest during the time the written consent was effective.

This form does not apply to property used to pay premiums. The form in section 10.188, *supra*, is used to reclassify assets used to pay premiums. The two forms can be combined into one form if desired. However, the consequences of such a combination should be carefully considered. Since this form applies only to the policy or the proceeds of the policy, and reclassifies the policy as the individual property of the other spouse, care must be taken with respect to the payment of premiums after execution of the written consent. If the written consent reclassifies a policy as the individual property of the other spouse, and marital property is subsequently used to pay a premium, it is arguable that the policy has become mixed property under section 766.61, with the result that it has a marital property

component. To avoid the argument of mixing, nonmarital property should be used by the other spouse to pay premiums.

Section 766.61(3)(e) applies to “a policy.” The statute does not expressly state whether it is limited to policies as they exist on the date the written consent is signed or whether the written consent may also apply to replacements of, additions to, or subdivisions of existing policies or new policies that may otherwise be acquired or issued in the future. This form applies to only a specific existing policy.

The differences between a revocable consent and irrevocable consent can be complex and thus should be considered. If the consent is revocable, it may be treated as an incomplete gift for tax purposes. If the consenting spouse can revoke at any time, he or she may have the ability to vest ownership of a portion of the life insurance policy in himself or herself.

➤ **Example.** On July 1, 1986, a husband signs a revocable written consent consenting to his wife’s son by a prior marriage as beneficiary of a certain policy. The written consent reclassifies the policy to be the wife’s individual property. The policy was issued after the determination date and the wife is the insured and the record owner.

Before the written consent was signed, the policy was marital property because the insured was the record owner and the policy was issued after the determination date. *See* Wis. Stat. § 766.61(3)(a). The effect of the written consent is to reclassify the policy as the wife’s individual property because the written consent so states. Wis. Stat. § 766.61(3)(e).

Assume that the husband revokes the consent on January 1, 1987. If section 766.61(3)(a) is applied literally, the policy is marital property after the revocation because the insured is the record owner and the policy was issued after the determination date. However, section 766.61(3)(e) states that unless the written consent provides otherwise, revocation does not operate to reclassify any property that was reclassified from the date of the consent to the date of revocation. Presumably, despite section 766.61(3)(a), the policy is the individual property of the wife immediately after revocation of the consent. But what is the effect of the payment of future premiums? Future premiums may be paid from nonmarital property or marital property. Generally, the special time-apportionment rules of section 766.61 apply to policies insuring spouses. However, section 766.61 does not contain any time-apportionment rules for a policy issued after the

determination date when the insured spouse is also the record owner. Thus, it is unclear whether the special time-apportionment rules of section 766.61 apply after revocation of a written consent.

If the special time-apportionment rules do not apply, the general property mixing rules contained in section 766.63(1) may apply. If some mixing rules apply, whether contained in section 766.61 or 766.63, the wife may be able to preserve the policy as her individual property by making sure that all premiums paid after revocation are paid with nonmarital property. Since the concept of section 766.61(3)(a) is that a life insurance policy issued after the determination date is marital property, a strong argument can be made that the policy in the example is individual property during the time the written consent is effective and is marital property after revocation, despite the classification of the property used to pay premiums after revocation.

If the consenting spouse can revoke the consent and thereby vest an ownership interest in the policy in himself or herself, a revocable consent may not be completely effective for tax purposes. The consent may have the effect of initially reclassifying the policy as the individual property of the wife, but the husband may be treated as a part owner of the policy for tax purposes during the period of the revocable consent to the extent he can vest an ownership interest in himself.

The above is just one example. The possible permutations and combinations that may arise under section 766.61 are numerous. One thing is certain: the preparation of a written consent form can be very complex.

## **K. Written Consent to Use of Property To Pay Life Insurance Premiums [§ 10.189]**

### **WRITTEN CONSENT TO USE OF PROPERTY TO PAY PREMIUMS**

I, (name), do hereby consent to the use of my interest in property to pay premiums on Policy #\_\_\_\_\_, which insures my spouse, (name).

This written consent is effective to reclassify all my interest in property used to pay premiums on said policy as the individual property of my spouse.



In view of the fact that this written consent is effective to reclassify my interest in such property as the individual property of my spouse, I understand that this written consent limits my rights in the policy.

This written consent is *(revocable)* *(irrevocable)*.

Dated: \_\_\_\_\_.

\_\_\_\_\_  
Witness

\_\_\_\_\_  
Consenting Spouse

➤ **Comment.** For a more complete discussion of written consent, see the comment to the form in section 10.188, *supra*.

Section 766.61(3)(e) provides for two types of written consents: a consent to the designation of another person as beneficiary; and a consent to the use of property to pay premiums. The former type of written consent is in section 10.188, *supra*. The form in this section is the latter type. The two types can be combined into one form if desired. The two types have been separated here to highlight their differences.

The consent form in this section may be revocable or irrevocable. If the form is revocable, adverse consequences may result if it is revoked. For example, assume that the written consent is being used to reclassify property as nonmarital property before premiums are paid on a life insurance policy owned by an irrevocable trust. If the consent is revoked, with the result that marital property is used to pay the premiums, both spouses may be considered to be grantors of the irrevocable trust for tax purposes.

If the written consent is revocable, it may be incomplete for tax purposes to the extent the consenting spouse can vest an ownership interest in himself or herself by revoking the consent. The tax consequences of using a written consent to reclassify property to pay premiums should be carefully considered.



# 11

## Family Law

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## **I. Scope of Chapter [§ 11.1]**

This chapter addresses the application of marital property rules or a comparison of those rules to the disposition of spouses' property when a marriage is dissolved. In addition, the marital property rules' effect on child support and maintenance is examined. The chapter also explains the effect and enforceability of marital property agreements as they relate to the dissolution of marriage. Finally, the chapter addresses nonmarital relationships and invalid marriages and their relationship to the marital property rules.<sup>1</sup>

## **II. Property Division at Dissolution [§ 11.2]**

### **A. In General [§ 11.3]**

#### **1. Property Division Rules [§ 11.4]**

The legal attributes of marriage have changed considerably from the view expressed by the Wisconsin Supreme Court in 1923 that "a marriage contract is a civil contract, but its essence is to define a status in society rather than to regulate control over property." *Roether v. Roether*, 180 Wis. 24, 27, 191 N.W. 576 (1923). In contrast, chapter 766 is titled "Property Rights of Married Persons; Marital Property." One of the purposes of the Wisconsin Family Code, chapters 765–768, is "to recognize the valuable contributions of both spouses during the marriage and at termination of the marriage by dissolution or death." Wis. Stat. § 765.001(2).

*Dissolution* is defined in the Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified as amended at chapter 766 and scattered

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189; all references to the United States Code (U.S.C.) and the Internal Revenue Code (I.R.C.) are current through Public Law No. 111-156 (excluding Pub. L. Nos. 111-148 and 111-152) (Apr. 7, 2010); and all references to the Wisconsin Administrative Code are current through Wisconsin Administrative Register No. 652 (Apr. 14, 2010) (eff. Apr. 15, 2010). Textual references to the Wisconsin Statutes are indicated as "chapter xxx" or "section xxx.xx," without the designation "of the Wisconsin Statutes."

sections of the Wisconsin Statutes) [hereinafter the Act or Wisconsin Marital Property Act], to mean the termination of the marriage by “decree of dissolution, divorce, annulment or declaration of invalidity or entry of a decree of legal separation or separate maintenance.” Wis. Stat. § 766.01(7). Different grounds for dissolution apply to the different types of actions. *See* Wis. Stat. § 767.315. Once the marriage is dissolved, marital property principles of ownership no longer apply; however, marital property rules apply as long as the parties are married, and marital property ownership may have a practical effect on couples undergoing a dissolution action.

Before the effective date of Wisconsin’s Marital Property Act, January 1, 1986, ownership of or title to property did not affect how a couple’s property was divided at dissolution, except for property received by gift or inheritance. *See* Wis. Stat. § 767.61. The same is true after the effective date of the Act. Classification of property, whether as marital property or nonmarital property (i.e., individual property or predetermination date property—that is, property acquired while the parties are married but before their determination date), does not determine how assets will be divided between the spouses if the marriage is dissolved. *Id.*; *Kuhlman v. Kuhlman*, 146 Wis. 2d 588, 432 N.W.2d 295 (Ct. App. 1988); *see also* June M. Weisberger, *The Marital Property Act Does Not Change Wisconsin’s Divorce Law*, Wis. B. Bull., May 1987, at 14. A spouse’s rights in property during the marriage are governed by chapter 766; a spouse’s rights in property at dissolution are governed by chapter 767.

Section 767.61 authorizes the court in a dissolution action to divide all property of the parties and to divest and transfer “title” accordingly. After the judgment of dissolution has been entered, the transfer of title by a property division transfers ownership to the recipient. Income and assets acquired after the divorce are the solely owned property of the owner and are not classified as marital property. *Luna v. Luna*, 183 Wis. 2d 20, 28–29, 515 N.W.2d 480 (Ct. App. 1994) (holding that circuit court erred in classifying husband’s income earned after dissolution as marital property).

The court begins the process of property division with the presumption that the property of the parties is subject to division. Wis. Stat. § 767.61. As is true of classification of an asset, title to the asset at the time of dissolution is irrelevant, except when one party is attempting to prove that an asset acquired by gift from a third party other than the

spouse or by inheritance, or assets traceable to such a gift or inheritance, is not subject to division, in which case title may become relevant. Assets so acquired are not divisible, unless the court finds that failure to divide the assets would create a hardship. Assets acquired by probate or nonprobate means on account of the death of another person, or assets traceable to assets so acquired, are likewise not divisible, absent hardship. *Id.*; *Asbeck v. Asbeck*, 116 Wis. 2d 289, 342 N.W.2d 750 (Ct. App. 1983); *see also infra* § 11.13. An exception to this general rule applies when the court finds that the character of the asset has changed, with the result that the asset is divisible. *See infra* §§ 11.13–15. The party asserting that an asset was acquired by gift or inheritance or with funds traceable to a gift or inheritance has the burden of proving its source. *Preuss v. Preuss*, 195 Wis. 2d 95, 536 N.W.2d 101 (Ct. App. 1995); *Brandt v. Brandt*, 145 Wis. 2d 394, 408, 427 N.W.2d 126 (Ct. App. 1988); *see also Steinmann v. Steinmann*, 2008 WI 43, 309 Wis. 2d 29, 749 N.W.2d 145 (discussing burden of proof for assets alleged not subject to division under marital property agreement); *Estate of Kobylski v. Hellstern (In re Estate of Kobylski)*, 178 Wis. 2d 158, 503 N.W.2d 369 (Ct. App. 1993) (discussing tracing principles and burden of proof in probate context); *Lloyd v. Lloyd (In re Estate of Lloyd)*, 170 Wis. 2d 240, 254, 487 N.W.2d 647 (Ct. App. 1992). It appears that a gift from the other party is divisible, whether the gift occurred before or after marriage. Interspousal gifts are divisible even though the transferred asset and the income from that asset may be classified as the individual property of the recipient under the Act's classification system. *See Wis. Stat. § 766.31(10)*. The different treatment of property acquired by gift or inheritance makes it useful to refer to such property as *nondivisible* property, which it is under ordinary circumstances, and all other property as *divisible* property. Some cases refer to nondivisible property as “exempt.”

Except for property acquired by gift or transfer at death, or purchased with funds so acquired, there is a presumption that all property is to be divided equally. Wis. Stat. § 767.61(3)(intro.). Under principles of equitable property division, a court may alter the presumptively equal division after consideration of the 13 factors set forth in section 767.61(3). The factors include the parties' age, health, skills, education, and length of time out of the job market; the value of the homemaker's contribution in caring for the home and children; and any other factor that in equity would entitle one spouse to more than one-half of the divisible property. *See Wis. Stat. § 767.61(3)(a)–(m)*. Recognition of the various contributions of each spouse who has worked in or outside

the home may be achieved by property division and by maintenance payments under section 767.56. Under Wisconsin's method of equitable division, the characterization of property as divisible does not necessarily mean that the property will be divided equally. By contrast, in some community property states, separate property is not divided and the division of community property and quasi-community property is strictly equal and without regard to equitable factors. *See infra* § 11.6.

In addition to awarding assets under section 767.61, the court may assign responsibility for payment of liabilities. Wis. Stat. § 766.55(2m); *see supra* ch. 6. A spouse may be assigned such responsibility even though he or she did not incur the debt. If an obligation is assigned to one spouse, the creditor has a direct cause of action against the spouse assigned the debt as well as against the spouse who incurred it. Wis. Stat. § 766.55(2m); *See infra* § 11.25. If the spouse who was not assigned responsibility pays the obligation, he or she may have a right of contribution against the spouse who was assigned responsibility for payment. *See infra* § 11.25.

After dissolution, with respect to a former marital property asset for which the decree makes no provision, each former spouse owns an undivided one-half interest in the asset as a tenant in common. Wis. Stat. § 766.75. However, it is highly unusual for a decree not to deal with an asset.

A legal separation is a dissolution of marriage, and a decree of legal separation has the legal attributes of a divorce in almost all respects. *See* Patricia K. Ballman, *Legal Separation: Is It a Termination of Marriage or a Suspension of Marriage?*, 25 Wis. J. Fam. L. 1 (2005).

## **2. Uniform Marital Property Act [§ 11.5]**

The Prefatory Note to the Uniform Marital Property Act (UMPA), 9A U.L.A. 103 (1998 & Supp. 2003), *reprinted infra* app. A, the uniform act on which the Wisconsin Marital Property Act is based, describes UMPA as an extension of the movement in common law property states toward the concept of sharing property at the death of a spouse or at the dissolution of the marriage. The Prefatory Note states that embodied in this movement is the equal sharing during the marriage of the economic rewards that flow from the personal efforts of either or both spouses during marriage. The interest of each spouse in a marital property asset



arises the instant the asset is acquired or created. It is not necessary for one spouse to wait for a gift from the other spouse, nor is it necessary to end the marriage to establish equal ownership. The heart of UMPA is economic equality throughout the marriage. *See* Prefatory Note to UMPA.

Wisconsin followed UMPA's principles in that no change in the law of divorce or other forms of dissolution was intended by the state's passage of the Marital Property Act. With the exception of one procedural amendment to chapter 767, *see* Wis. Stat. § 767.331, no statutory change in the law concerning dissolution resulted from the adoption of the Marital Property Act. The UMPA Prefatory Note explains the role of property law at the dissolution of a marriage:

The Act takes the parties "to the door of the divorce court" only. It leaves to existing dissolution procedures in the several states the selection of the appropriate procedures for dividing property. On the other hand the Act has the function of confirming the *ownership* of property as the couple enters the process. Thus reallocation of property derived from the effort of both spouses during the marriage starts from a basis of equal undivided ownership that the spouses share in their marital property.

Wisconsin did not enact all UMPA sections that affect dissolution. For example, the state omitted UMPA section 13, concerning the valuation of deferred employment benefits, and UMPA section 17, concerning the treatment of certain property at dissolution.

When the Act first became effective, there was some confusion as to whether marital property classification rules would have an impact on dissolution actions. In *Kuhlman v. Kuhlman*, 146 Wis. 2d 588, 432 N.W.2d 295 (Ct. App. 1988), the circuit court determined that all property of the parties was classified as marital property. The circuit court divided the property equally, on the ground that chapter 766 superseded the equitable-division provisions of section 767.255 (now section 767.61). The court of appeals found that the Act does not determine property division and remanded the case for property division in accordance with the equitable-property division standards of section 767.255 (now section 767.61).

Thus, UMPA and the Wisconsin Marital Property Act are property statutes. Nevertheless, how an asset is owned or classified does not alter a divorce court's authority to disregard title or ownership in making a

property division. *See* UMPA § 17 cmt.; Wis. Stat. Ann. § 766.75 Legis. Council Notes—1985 Wis. Act 37, §§ 141–143 (West 2009). Assets that are excluded from property division are excluded by authority of section 767.61, not because of their classification under chapter 766.

In *Gardner v. Gardner*, 190 Wis. 2d 216, 236–37, 527 N.W.2d 701, 708 (Ct. App. 1994), the court of appeals, citing *Kuhlman*, reiterated the principle that classification under the Marital Property Act has no relation to how assets are divided upon dissolution of the marriage.

### **3. Comparison of Wisconsin to Other Community Property States [§ 11.6]**

The various community property states, as well as common law property states, apply several approaches to the division of property at dissolution. Since none of them is completely analogous to the approach in Wisconsin, extreme caution must be exercised in considering case law from other community property states.

In California, Louisiana, and New Mexico, the spouses' community property is divided equally, and in California, quasi-community property, which is property that would have been community property if it had been acquired in California, is also divided equally; in these states, each spouse receives his or her separate property. *See* Cal. Fam. Code Ann. §§ 2550–2660 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot); La. Civ. Code Ann. Art. 2336 (West, WESTLAW current through 2009 regular session); N.M. Stat. Ann. § 40-4-3 (West, WESTLAW current through laws effective March 9, 2010 of the Second Session of the 49th Legislature (2010)); *Michelson v. Michelson*, 520 P.2d 263 (N.M. 1974). A contested property division in one of these states would focus on classification of assets, and in turn on tracing, since equitable factors are not relevant. A spouse may attempt to show that property is his or her separate property to be awarded all of it and may attempt to show that the other spouse's allegedly separate property is community property to receive one-half. California is unique in that it also has a detailed system for assigning responsibility for payment of debts incurred while the parties were married but residing separately.

By contrast, Arizona, Idaho, Nevada, Texas, and Washington do not divide community property assets equally but rather provide for an equitable division of community property assets at dissolution. Ariz. Rev. Stat. Ann. § 25-318 (West, WESTLAW current through legislation effective February 9, 2010 of the Sixth Special Session, and legislation effective April 5, 2010 of the Second Regular Session of the Forty-Ninth Legislature (2010)); Idaho Code § 32-712 (West, WESTLAW current through (2010) Chs. 1-161 and HJR's 4, 5, and 7 that are effective on or before March 29, 2010); Nev. Rev. Stat. § 125.150 (West, WESTLAW current through the 2007 74th Regular Session and the 25th Special Session (2008) of the Nevada Legislature and technical corrections received from the Legislative Counsel Bureau through the 25th Special Session (2008)); Tex. Fam. Code Ann. § 7.001 (West, WESTLAW current through end of 2009 Regular and First Called Session of the 81st Legislature); Wash. Rev. Code Ann. § 26.09.080 (West, WESTLAW current with 2010 legislation effective through March 16, 2010). In these states, separate property is awarded to the owner, except that in Washington separate property may also be equitably divided (although whether an asset is separate or community property is a factor in arriving at an equitable division). Wash. Rev. Code Ann. § 26.09.080 (West, WESTLAW current with 2010 legislation effective through March 16, 2010). In these states, courts may also divide certain types of assets equitably notwithstanding that an asset might not be community property; such non-community property could be homestead property, co-owned property, or property acquired while the parties resided in another state that would have been community property if acquired in the state in which the parties resided when the dissolution occurred. Wash. Rev. Code Ann. § 26.09.080 (West, WESTLAW current with 2010 legislation effective through March 16, 2010); *see also Washington Community Property Deskbook* § 5.40 (3d ed. 2003); W.S. McClanahan, *Community Property Law in the United States* 244–50 (1982 & Supp. 1992). There are also variations in the application of equitable factors.

In all community property states, each spouse has an undivided one-half interest in each community property asset, but each asset need not itself be divided upon dissolution. *See supra* § 2.22. A court in a state requiring equal division of community property may divide the aggregate of all community property so that each spouse receives an equal share of the total. If an equitable division is allowed, then different shares of the aggregate of the community property or of the community and separate property may be awarded to the parties.

Since Wisconsin's property-division system at dissolution includes equitable division of both marital property assets and nonmarital property assets, Washington appears to have the system closest to Wisconsin's. However, an important distinction is that Washington treats both inherited property and property brought to the marriage as separate property, but there is no distinction in the way assets of each type are treated at dissolution. Wash. Rev. Code Ann. § 26.09.080 (West, WESTLAW current with 2010 legislation effective through March 16, 2010). Wisconsin, on the other hand, treats these two types of individual property differently at dissolution. Property brought to the marriage is subject to division, but property acquired before or after marriage by gift or inheritance, or property acquired with funds received by gift or inheritance, is only divided if failure to do so would result in a hardship for the other spouse or the children. Wis. Stat. § 767.61; *See infra* §§ 11.10, .13.

Because of the wide variation in property-division rules in other community property states, and Wisconsin's well-established rule that classification under the Act is not a factor in determining property division, case law from other community property states concerning property division is of limited value.

#### **4. Previous Representation by Counsel [§ 11.7]**

An attorney who previously represented both spouses in various matters may be asked by one of the spouses to represent that spouse in a divorce action. This may be economical if the attorney is familiar with the client's business or other financial affairs. However, if significant matters involved in a prior dual representation are relevant to the divorce, written consent from the other spouse to the subsequent representation is necessary. *See infra* ch. 14.

In addition, the attorney must be alert to possible conflicts of interest that did not arise under the common law property system. For example, the attorney who represents a business corporation in which one spouse is employed, the stock of which is classified as the spouses' marital property, may be asked to represent only the employed spouse in a divorce. In representing the business, the attorney may have acquired confidential information, and agreeing to represent either spouse in a divorce may, depending on the particular circumstances, conflict with the attorney's prior representation. *See, e.g., Mathias v. Mathias*, 188 Wis.

2d 280, 525 N.W.2d 81 (Ct. App. 1994) (holding that prior estate planning for husband was “substantially related” to divorce, and husband’s attorneys were precluded from representing wife in dissolution). In such a case, unless both spouses consent, the attorney must decline to represent either spouse. *See Woods v. Superior Court*, 197 Cal. Rptr. 185 (Ct. App. 1983). *But see Friedman v. Friedman (In re Marriage of Friedman)*, 122 Cal. Rptr. 2d 412 (Ct. App. 2002) (holding that wife could not avoid prenuptial agreement even though same law firm represented both spouses in estate planning and represented only husband with respect to agreement, because wife was attorney and no duress or unfair advantage was found).

## **B. Application of Principles of Equitable Division to Various Types of Property [§ 11.8]**

### **1. Marital Property [§ 11.9]**

The only kind of property that is nondivisible at dissolution is property that is acquired by gift from a third party or by reason of the death of another or that is purchased with funds so acquired (although even this property is divisible if hardship would otherwise result). Wis. Stat. § 767.61(2). In general, such nondivisible property is classified as individual property. Wis. Stat. § 766.31(7)(a); *See infra* § 11.13.

It follows that marital property assets are divisible at dissolution of the marriage. The determination of what assets are to be divided is made as of the date of dissolution, unless “special circumstances” exist. *Sommerfield v. Sommerfield*, 154 Wis. 2d 840, 851, 454 N.W.2d 55 (Ct. App. 1990); *see also Long v. Long*, 196 Wis. 2d 691, 539 N.W.2d 462 (Ct. App. 1995) (holding that income earned and spent during pendency of dissolution was marital property but could not be divided as an asset). Although there is a presumption that divisible property is to be divided equally, the court may depart from the equal division after considering the equitable factors of section 767.61(3)(a)–(m).

The burden of proving that property is nondivisible at dissolution is on the party attempting to exclude the property from division. *Steinmann*, 2008 WI 43, ¶ 26, 309 Wis. 2d 29; *Preuss*, 195 Wis. 2d at 101; *Brandt*, 145 Wis. 2d at 408–09; *Popp v. Popp*, 146 Wis. 2d 778, 786–87, 432 N.W.2d 600 (Ct. App. 1988). Although property received

by gift or inheritance is entitled to a statutory presumption of nondivisibility, property classified as individual by a marital property agreement is not. *Steinmann*, 2008 WI 43, ¶ 38, 309 Wis. 2d 29. Once property has been determined to be part of the divisible estate, there need be no showing of hardship to divide it. *Brandt*, 145 Wis. 2d at 417.

One commentator has posited a theory that a marital property agreement classifying spouses' assets as marital property for all purposes except dissolution, thereby obtaining the tax benefits of community property ownership at death, will not subject otherwise nondivisible assets to division at dissolution. Carl J. Rasmussen, *Divorce Provisions in Opt-in Marital Property Agreements*, Wis. Law., Apr. 1994, at 15. The dissolution and tax ramifications of this theory are uncertain. See *supra* § 11.3.

## **2. Property Brought to Marriage Not Acquired by Gift from Third Party or by Reason of Another Person's Death [§ 11.10]**

Property brought to the marriage, whether inherited or received by gift or acquired by other means, is classified as individual property or as predetermination date property if the marriage occurred before January 1, 1986, or while the parties resided in another state. Wis. Stat. § 766.31(6) (defining individual property). However, these two "types" of individual or predetermination date property—that is, property brought to the marriage that was inherited or received by gift and property brought to the marriage that was acquired by other means—are treated differently at dissolution. See Wis. Stat. § 767.61(2)(a).

At dissolution, property brought to the marriage that was not acquired as a gift from a third party or inherited, or was not purchased with funds so acquired or traceable to such funds, is subject to division under section 767.61, although the extent of such property is one factor that may be considered in awarding the spouse who owns such property a greater share of the estate. Wis. Stat. § 767.61(3)(b); see *Hokin v. Hokin*, 231 Wis. 2d 184, 194–95, 605 N.W.2d 219 (Ct. App. 1999) (holding that court was not required to divide deferred employment benefits using the "coverture" fraction found in section 766.62(2) but was not prohibited from doing so). On the other hand, the property one spouse acquires by gift or inheritance before or after the marriage is excluded from the

property division, assuming it is traceable to identifiable assets at the time of the dissolution and has not been transmuted. *See infra* § 11.13. Such property is awarded to the owner spouse unless it would be a hardship to the other spouse or the children of the parties to do so. Wis. Stat. § 767.61(2)(b); *Doerr v. Doerr*, 189 Wis. 2d 112, 121–25, 525 N.W.2d 745 (Ct. App. 1994).

Persons who inherit or are given property while they are not married might not keep separate records for such property. If marriage is not contemplated, there is no reason for a person not to mix such property with property acquired by other means. When mixing has occurred before marriage, and a person wishes to retain the property in the event of divorce, it may be appropriate to use a marital property agreement before marriage to confirm the identity of the gift or inheritance portion of a person's assets. *See supra* § 7.32.

### **3. Property Acquired While Married and Before Determination Date Other Than by Gift from Third Party or by Reason of Another Person's Death [§ 11.11]**

Assets that spouses acquire while they are married but before their determination date—that is, while the spouses resided in another common law state or while they resided in Wisconsin before January 1, 1986—are neither marital property nor individual property but rather a type of predetermination date property. The spouses' rights in such property were unchanged by the passage of chapter 766. Wis. Stat. § 766.31(8). Unless a spouse can prove that an asset that is predetermination date property was acquired by gift from a person other than the other spouse or was acquired by reason of the death of another person, or was purchased with property so acquired, the asset is divisible in a property division at dissolution of the marriage. Wis. Stat. § 767.61(2)(a).

The fact that spouses acquire an ownership interest during marriage in marital property assets acquired after the determination date but do not acquire a present interest in similar property acquired while the spouses are married but before the determination date does not affect the spouses' rights in assets divided at dissolution. Section 767.255(5e) of the original Marital Property Act treated assets that would have been marital

property if acquired after the determination date in the same manner as marital property upon dissolution. The inclusion of this subsection might have been interpreted to mean that predetermination date property that would have been classified as marital property under the Act would have to be divided equally at dissolution. This subsection was deleted by 1985 Wisconsin Act 37 [hereinafter 1985 Trailer Bill], to avoid confusion concerning the Act's effect on property division at divorce, since a change in the court's power to equitably divide property was not intended. *See* 1985 Wis. Act 37, § 150. Links to acts amending the Wisconsin Marital Property Act are available in appendix B, *infra*.

➤ **Note.** Section 767.255 was repealed and recreated as section 767.61, effective January 1, 2007.

#### **4. Property Acquired by Gift from Third Party or by Reason of Another Person's Death [§ 11.12]**

##### **a. In General [§ 11.13]**

Section 767.61(2)(a)–(b) provides that assets received by inheritance or by gift to a spouse from a third party, before or after marriage, or assets traceable to such assets, are excluded from property division unless the court finds that failure to divide the asset will result in a hardship for the other spouse or the parties' children. Likewise, funds or other assets acquired on account of the death of another person, including life insurance proceeds, death benefits payable by a deferred-employment-benefit plan, individual retirement account (IRA) proceeds, property acquired by right of survivorship, trust distributions, bequests, inheritances, funds received by payable-on-death designation, or any other transfer under chapter 705 are nondivisible, unless the court finds that failure to divide the asset will result in a hardship for the other spouse or the parties' children. Wis. Stat. § 767.61(2)(b); *see also Doerr v. Doerr*, 189 Wis. 2d 112, 525 N.W.2d 745 (Ct. App. 1994). If awarding nondivisible assets to the owner would result in a hardship to the other spouse or the children, the court may award sufficient nondivisible property to the other spouse to avoid the hardship. Wis. Stat. § 767.61(2)(b); *see also Grumbeck v. Grumbeck*, 2006 WI App 215, 296 Wis. 2d 611, 723 N.W.2d 778 (holding that court may not make de facto division of gifted property by awarding a majority of divisible assets to nonowning spouse without showing of hardship); *Popp*, 146



Wis. 2d at 790–92; *Asbeck v. Asbeck*, 116 Wis. 2d 289, 295, 342 N.W.2d 750 (Ct. App. 1983). This rule is unchanged by the Act.

A spouse attempting to exclude from a property division assets acquired by gift or inheritance has the burden of proof that an asset is not subject to division. *Preuss*, 195 Wis. 2d at 101; *Brandt*, 145 Wis. 2d at 408. Once the party attempting to exclude the asset has made a prima facie showing that the asset is traceable to property acquired by gift or inheritance, the burden shifts to the other party to rebut the evidence by showing that the character of the asset has changed from nondivisible to divisible. *Brandt*, 145 Wis. 2d at 408–09; *Spindler v. Spindler*, 207 Wis. 2d 327, 558 N.W.2d 645 (Ct. App. 1996); *Trattles v. Trattles*, 126 Wis. 2d 219, 376 N.W.2d 379 (Ct. App. 1985); *see also* Neal Nettesheim, *Gifted and Inherited Property: To Divide or Not Divide?*, 10 Wis. J. Fam. L. 127 (1990).

Two key concepts have evolved in the analysis of whether a particular asset is subject to division: *character* and *identity*. The concept of character is loosely analogous to the classification and reclassification of property when a dissolution court determines whether an asset that was not subject to division when one spouse acquired it has changed so that it is subject to division. *See supra* ch. 3. However, the classification of property under marital property law is not synonymous with a determination of its character for purposes of property division at dissolution, and property is not classified in the dissolution proceeding. The rationale underlying the application of marital property law to the classification of assets is distinct from the principles applied in dividing assets at dissolution, and cases decided after the Marital Property Act became effective have made it clear that an asset's classification does not determine its division at dissolution.

If the court determines that a nondivisible asset has not changed its character, then the court must determine if it can be identified. The concept of identity is loosely analogous to tracing principles applicable to mixed property and whether an asset in existence at the time of divorce can be proved to have been acquired with funds traceable to an asset that was nondivisible when it was acquired. Otherwise nondivisible assets that have lost their character or have not retained their identity are subject to property division at dissolution. *Preuss*, 195 Wis. 2d at 103–04.

The Wisconsin Court of Appeals sought to clarify the line of cases dealing with character and identity in *Derr v. Derr*, 2005 WI App 63, 280 Wis. 2d 681, 696 N.W.2d 170. The court found those terms confusing and largely unhelpful when dealing with whether an asset is subject to division in the dissolution of a marriage. Instead, the court focused on tracing, as opposed to identity, which it described as “nothing more than the exercise of following an asset trail. If an asset, or component part of an asset, can be traced to a source, we then rely on *other* principles and rules to determine whether the traced asset is divisible or non-divisible.” *Id.* ¶ 19. The party wishing to exclude an asset from division has the burden of tracing the existing asset to a nondivisible source. *Id.* ¶¶ 11, 17 (citing *Brandt v. Brandt*, 145 Wis. 2d 394, 427 N.W.2d 126 (Ct. App. 1988)); *see also Krejci v. Krejci*, 2003 WI App 160, 266 Wis. 2d 284, 667 N.W.2d 780.

The *Derr* court also rejected the term character in favor of *donative intent* when determining whether an asset has changed from a nondivisible asset to one that is subject to division. *Derr*, 2005 WI App 63, ¶ 24, 280 Wis. 2d 681. After surveying the many cases dealing with change of character or donative intent in making a gift of a nondivisible asset to the pot of marital assets subject to division, the court in this case held that the husband had not possessed the requisite donative intent. The husband’s parents gave him a parcel of commercial real estate, which he kept in his sole name. Even though he had executed a mortgage on the building for a loan, the proceeds of which were used for the benefit of the family, and payments were made with marital funds, he did not intend to make a gift to the marriage. *Id.* ¶ 62. However, the debt was divisible. *Id.* ¶¶ 48–49; *see also* Marta T. Myers, *Gifted and Inherited Property after Derr: “Tracing” and “Donative Intent” Are In; “Character” and “Identity” Are Out*, 26 Wis. J. Fam. L. 37 (2006); Brett R. Turner, *Tracing, Transmutation and the Language of Law*, 17 Divorce Litig. 89 (2005).

## **b. Character [§ 11.14]**

Cases dealing with character focus on how the asset is held or titled and whether it was treated as separate by the owner during the marriage. A change in the classification or character of the asset as a result of the owner’s conduct is sometimes referred to as *transmutation*. It is relevant whether the asset, or assets traceable to the asset, originally acquired by gift or inheritance are still in the name of the spouse who originally

acquired the asset. If the spouse who originally acquired the asset keeps it separate from the spouses' other assets and continually treats it as being solely owned, it retains its character. *See, e.g., Popp*, 146 Wis. 2d at 788 (discussed *infra*); *Gardner v. Gardner*, No. 92-1258, 1993 WL 331496 (Wis. Ct. App. Sept. 2, 1993) (unpublished opinion not citable per section 809.23(3)); *see also Lloyd*, 170 Wis. 2d at 259 (discussing character in probate context). Courts in cases involving real estate in which title changed from the name of the spouse who acquired the nondivisible real estate, or the funds used to acquire it, to the names of both spouses have held that the real estate changed its character and became divisible; *see Steinmann*, 2008 WI 43, ¶ 58, 309 Wis. 2d 29 (holding that allegation of no donative intent in titling property jointly not proved); *Bonnell v. Bonnell*, 117 Wis. 2d 241, 344 N.W.2d 123 (1984) (holding that wife changed title to inherited cottages to a joint tenancy with her husband, thereby changing character and subjecting cottages to division); *Weiss v. Weiss*, 122 Wis. 2d 688, 691–94, 365 N.W.2d 608 (Ct. App. 1985) (holding that funds received by gift used for down payment on joint real estate were divisible). Whether types of assets other than real estate or titled assets have changed character depends on the nature of the asset and the conduct of the acquiring spouse. *See also Rumpff v. Rumpff*, 2004 WI App 197, 276 Wis. 2d 606, 688 N.W.2d 699 (holding that gifted property was no longer nondivisible individual property at time of divorce and upholding equal division; court did not address hardship).

Donative intent is necessary to change the character of an asset from nondivisible to divisible. *Steinmann*, 2008 WI 43, ¶ 34, 309 Wis. 2d 29; *Brandt*, 145 Wis. 2d at 410–11. For example, in *Popp v. Popp*, 146 Wis. 2d 778, 432 N.W.2d 600 (Ct. App. 1988), the husband had received a gift of stock in a family corporation during the marriage. He had used corporate funds to purchase artwork, some of which was used in the family home. He did not treat the artwork as his solely owned property, thus making it possible to infer donative intent. The court found that the artwork was contributed to family use and was divisible, while the stock received by gift was not.

Donative intent can usually be inferred from a party's actions. For example, the husband in *Finley v. Finley*, 2002 WI App 144, 256 Wis. 2d 508, 648 N.W.2d 536, placed inherited funds in a joint bank account, and a presumption arose that the character of the funds was changed from the husband's individual property to funds having a family or marital purpose, thus making the IRAs purchased with those funds divisible

when the parties later divorced. The evidence showed that these funds were part of an overall plan of retirement planning for the spouses, and the presumption was not rebutted.

Another example of donative intent involved a change in the title of real estate to the names of both spouses. In *Steinmann*, the wife used her funds, classified as her individual property by a marital property agreement, to purchase real estate titled jointly. The court held the real estate divisible. *Steinmann*, 2008 WI 43, ¶ 2, 309 Wis. 2d 29. Similarly, in *Weiss*, 122 Wis. 2d at 692–94, the husband had used a \$5,000 gift as a down payment on a home placed in joint tenancy with his wife. The court found this sufficient to establish donative intent, and it held that the entire value of the house was divisible. In *Trattles v. Trattles*, 126 Wis. 2d 219, 376 N.W.2d 379 (Ct. App. 1985), the wife had received gifts of cash that were used for ordinary living expenses, household items, and mortgage payments and improvements on jointly held real estate. The court stated that the mixing of nondivisible assets and other assets created a presumption of donative intent, which in that case was not rebutted. Mixing can cause the character of property to change even if the circuit court does not make a specific finding that the donor spouse had donative intent. *Id.* at 224. Once the court determines that the character of the property has changed from property not ordinarily subject to division to divisible property, then it is not necessary to determine its “identity” (by tracing the inherited portion). *Id.* at 227–28; see also Joan F. Kessler, et al., *The Law of Tracing Separate Property: Where Should Wisconsin Be Going?*, 21 Wis. J. Fam. L. 71 (2001); Joan F. Kessler, *Transmutation: Finding Extra Property to Divide in Divorce*, Wis. Law., Aug. 1990, at 13; Brett R. Turner, *Changing Horses in Midstream: The Doctrine of Transmutation*, 3 Equitable Distribution Alert 5 (May 1991); Brett R. Turner, *Transmutation by Commingling and the Process of Tracing*, 3 Equitable Distribution Alert 13 (June 1991).

The creation of joint ownership of a bank account in the names of both spouses is not necessarily conclusive as to a change of character. See *supra* § 3.14. For example, the wife in *Zirngibl v. Zirngibl*, 165 Wis. 2d 130, 477 N.W.2d 637 (Ct. App. 1991), placed funds acquired by gift before marriage in a joint bank account for the purchase of a home to be held in joint tenancy. However, the husband titled the house in his sole name. The court found that the wife’s deposit to the joint bank account was a conditional gift, and since the condition (i.e., the purchase of a home held in joint tenancy) was not met, she was entitled to recover the

funds intended for the purchase of joint real estate when the parties' assets were divided at dissolution. *Id.* at 135–37. In *Weberg v. Weberg*, 158 Wis. 2d 540, 463 N.W.2d 382 (Ct. App. 1990), the husband had placed otherwise nondivisible funds in a joint account. These funds were not, however, commingled with other funds, and the court found that the funds were only in a joint account to protect the wife if the husband died and that there was no present donative intent. Therefore, no change in character was found. *Id.* at 550–51. Similarly, the wife in *Brandt v. Brandt*, 145 Wis. 2d 394, 427 N.W.2d 126 (Ct. App. 1988), had inadvertently placed inherited funds in a joint brokerage account, but she placed them in her own name as soon as the mistake was discovered. No change of character occurred with respect to that account or to the same funds later transferred to an account held by a bank. The brokerage account appeared to have been treated like a bank account for tracing purposes. Unlike in *Weberg*, however, in *Brandt*, other divisible funds were placed into the account into which nondivisible funds had been deposited. Through “countless transactions,” these nondivisible funds could not be traced and lost their identity, even though they had not lost their character. *Brandt*, 145 Wis. 2d at 413; *see also supra* §§ 2.293, 3.14. *Brandt* and *Weberg* illustrate the interaction between the application of character and identity concepts and how such application affects the divisibility of an asset. *See also* Neal Nettesheim, *Gifted and Inherited Property Character and Identity*, 8 Wis. Law. Marital Prop. F. 11 (1991).

In *Spindler v. Spindler*, 207 Wis. 2d 327, 558 N.W.2d 645 (Ct. App. 1996), the wife attempted to prove that her labor and the expenditure of marital property funds to maintain the husband's inherited cottage had changed its character, entitling her to a portion of its increase in value during marriage. The property had been in the husband's name since he acquired it, so its identity did not change. *Id.* at 339. The court of appeals overruled the circuit court's finding that the property had lost its separate character, given the testimony of the appraiser that the increase in value of the property overall resulted solely from an increase in the value of the land and that the improvements' value had not grown. The court held that any increase in value as a result of the nonowning spouse's efforts must be substantial to change the asset's character. *Id.* at 339–40. However, the marital property funds expended for upkeep, which the court stated could be readily ascertained, were subject to division, and the court assigned the balance of the cottage's value to the husband. *Id.* at 340. The court of appeals remanded the case to the

circuit court to determine whether there would be a hardship to the wife if the value were not divided. *Id.* at 341.

The *Spindler* case was distinguished by the court in *In re Czerneski*, 330 B.R. 240 (Bankr. E.D. Wis. 2005), in which the debtor husband was attempting to claim a portion of the value of an individual property asset owned by the debtor wife. The court rejected the husband's position, observing that payment of property taxes did not entitle the husband to a property interest, citing *Krueger v. Rodenberg*, 190 Wis. 2d 367, 527 N.W.2d 381 (Ct. App. 1994), and that any rights to the property under divorce law, such as awarding otherwise nondivisible property to the nonowning spouse on account of hardship, did not apply in the bankruptcy context, which looks solely to property law. *See supra* ch. 4; *see also* David R. Knauss, Comment, *What Part of Yours is Mine?: The Creation of a Marital Property Ownership Interest by Improving Nonmarital Property Under Wisconsin's Marital Property Law*, 2005 Wis. L. Rev. 855.

➤ **Comment.** Had mixing occurred in *Czerneski* as a result of the use of marital property funds to pay real estate taxes on the wife's real estate, the husband could have claimed his interest exempt. The couple could then have excluded a greater value from their combined bankruptcy estates, which would have preserved the value for the debtors rather than their creditors.

In *Fowler v. Fowler*, 158 Wis. 2d 508, 463 N.W.2d 370 (Ct. App. 1990), inherited stock that was exchanged for other stock did not change character, but cash gifts deposited in a joint account did. The wife had inherited AT&T stock. When AT&T was required to divest itself of assets, the stock was exchanged for shares of various other companies. The court found that the exchange did not result in a change in the stock's character. *Id.* at 516. However, gifts of cash that were deposited in the parties' joint bank account along with other divisible funds had been so commingled as to lose their character, making them fully divisible. *Id.* at 517–18. The court found the joint account was divisible in character, whereas the courts in *Brandt* and *Weberg* held that the joint accounts in those cases retained their nondivisible character.

A single asset can have a character that has both a divisible component and a nondivisible component. In *Torgerson v. Torgerson*, 128 Wis. 2d 465, 383 N.W.2d 506 (Ct. App. 1986), only the down payment on rental real estate consisted of the wife's inheritance;

mortgage payments and maintenance expenses had been paid from the rent and from the spouses' earnings from employment. Title remained in the wife's name. The husband made no claim to the down payment, and that amount was returned to the wife. The parties did not ask the court to determine whether the down payment had lost its character. The court divided the value of the asset in excess of the down payment.

*Schwegler v. Schwegler*, 142 Wis. 2d 362, 364–66, 417 N.W.2d 420 (Ct. App. 1987), also involved an asset with possible divisible and nondivisible components. The husband had received real estate by gift before the marriage and had built a house on it using other funds, also before the marriage. The circuit court had awarded the wife one-half of the appreciation in the house that had occurred during the marriage. The husband argued that he should receive the entire value of the house and land. The court of appeals remanded the case to the circuit court to determine whether the house was an asset with separate character that would be divisible even though the land was not.

*Wierman v. Wierman*, 130 Wis. 2d 425, 387 N.W.2d 744 (1986), demonstrates the well-settled rule that marital property classification rules do not govern property division. The wife had received a gift of an interest in a real estate partnership. The partnership was managed by the wife's father. Except for amounts needed to pay income taxes, the profits from real estate sales were retained in the partnership and reinvested. Neither spouse's labor contributed to the increase in the partnership's value. *See infra* § 11.16. The court found that no mixing of nondivisible and other assets had occurred, so the character of the partnership interest was not changed. However, the court did not address the wife's share of accumulated partnership income, which would have been added to the wife's partnership account each year. Under classification principles, the wife's share of accumulated partnership income would be marital property and subject to division. *See supra* § 2.51, *infra* § 11.17. It appears that even though the wife's share of the income from the partnership would have been marital property, the court treated it as nondivisible because it remained in the partnership, thereby preserving its character and identity for divorce purposes. Also, the fact that neither spouse's efforts contributed to the acquisition of funds retained in the partnership may have been a consideration in the award of the entire value of the partnership interest to the wife, even though those funds would have been marital property. *Wierman*, 130 Wis. 2d at 441.

*Lendman v. Lendman*, 157 Wis. 2d 606, 460 N.W.2d 781 (Ct. App. 1990), also concerned income retained by a business entity that originally would have been characterized as nondivisible. The husband had formed a corporation, contributed \$8,500 of inherited funds as the initial capital, and loaned the corporation approximately \$25,000 of inherited funds. The corporation incurred debt to acquire the business and reduced the debt from corporate income as it was earned. The parties stipulated that the value of the stock in the corporation increased during the marriage by the amount of the debt reduction. The court found that the initial capital maintained its nondivisible character, but the increase in value of the corporation attributable to the debt reduction was divisible. *Id.* at 610–12. See section 11.16, *infra*, for further discussion of *Lendman* and the effect of labor on the value of an entity. If the parties had not agreed on the value of the corporation and the component part of the value that represented inherited funds, it is not clear how the court could have determined what part of the asset's value had retained its inherited character.

In *Arneson v. Arneson*, 120 Wis. 2d 236, 355 N.W.2d 16 (Ct. App. 1984), the husband worked in his family-owned business. He received some of his stock in the business by gift and purchased some of the stock using dividends generated by the stock and distributed to him. The court distinguished between the asset, which was acquired by gift and retained its character, and the income the asset produced, which was earned and not acquired by gift. It did not divide the stock acquired by gift but did divide the stock purchased with dividends. *Id.* at 245–46; See *infra* § 11.17. These earnings were at all times divisible in character. The appreciation in the stock's value, resulting from the husband's efforts or otherwise, was not addressed.

Similarly, the court in *Preuss*, 195 Wis. 2d at 102–03, held that the offspring of cattle acquired by gift were not themselves a gift excludable from division. The original cattle, which the wife had received by gift from her father, no longer existed. Therefore, all existing cattle had been acquired other than by gift and were subject to division.

The character of distributions from a trust established by a third party was addressed in *Friebel v. Friebel*, 181 Wis. 2d 285, 510 N.W.2d 767 (Ct. App. 1993). The court distinguished distributions of trust income from the dividend income received by the shareholder spouse in *Arneson*. Unlike the income at issue in *Arneson*, the income from assets in the trust in *Friebel* was not income from an asset owned by a spouse;



the trust had legal ownership of the assets, and the beneficiary had no right to demand possession or to dispose of the assets. Thus, when the trust funds were distributed, they were a gift at that time from the settlor. *Id.* at 294–95. It was immaterial whether the distributions were from the trust’s principal or from the trust’s income. Because the wife had kept these distributions in a separate account and there was no evidence of donative intent to change ownership, the distributions retained their character. *Id.* at 298. However, income earned on the distributions in the separate account were subject to division. *Id.* at 297. It was not clear from the record how much of the wife’s account was derived from gains on sales of appreciated investments, and the court of appeals remanded for that determination. The court stated that gains resulting from appreciation are usually not divisible, citing *Wierman*, but that income that is separate from a gift is divisible. *Id.*; see also *Grohmann v. Grohmann*, 189 Wis. 2d 532, 525 N.W.2d 261 (1995) (holding that undistributed income from grantor trust established by parent with assets received by gift could be used to establish amount of child support, even though trustee had discretion to distribute income); Patricia K. McDowell, *Trust Issues in Divorce*, 14 Wis. J. Fam. L. 55 (1994).

### c. Identity [§ 11.15]

If the court determines that the character of an asset has not changed, it must determine whether the nondivisible asset can be identified. The concept of identity refers to whether the asset acquired by gift or inheritance can be traced to a particular asset in existence at the time of dissolution. *Brandt*, 145 Wis. 2d at 411–13. The asset sought to be excluded must be in existence at the time of dissolution, or there must be an asset in existence that is traceable to the gift. *Preuss*, 195 Wis. 2d at 103–04 (holding that inherited funds had been expended and could not be excluded by the wife); see also *Lloyd*, 170 Wis. 2d at 268 (applying character and identity principles in probate context and holding that transfer of predetermination date funds into joint bank account held by both spouses changed character of funds to marital property); *Estate of Kobylski*, 178 Wis. 2d 158. The nondivisible character must first be determined to have been retained before identity becomes an issue. *Steinmann*, 2008 WI 43, ¶¶ 34–35, 309 Wis. 2d 29 (no tracing necessary when donative intent was found). For a discussion of tracing principles, see chapter 3, *supra*.

In *Bonnell v. Bonnell*, 117 Wis. 2d 241, 344 N.W.2d 123 (1984), and *Weiss v. Weiss*, 122 Wis. 2d 688, 365 N.W.2d 608 (Ct. App. 1985), both of which involved real estate held by the spouses in joint tenancy, the inherited property or the funds received by gift could easily be traced. However, the transmutation or change in character of the original asset made tracing immaterial. Once an asset is determined to be divisible, its source becomes irrelevant.

In *Friebel*, discussed in section 11.14, *supra*, the court concluded that the character of assets in the wife's investment account had been retained, but that the interest income on the account was subject to division. The circuit court had held that the assets were commingled by the retention of interest income in the account, but the court of appeals disagreed. The court estimated that no more than five percent of the account could have been income. Since the wife agreed that any withdrawals could be considered to be from the funds she had received by gift, the income could be readily ascertained from the account records. On remand the court was directed to subtract the full value of divisible property (i.e. the income on the account) and award the balance to the wife. *Friebel*, 181 Wis. 2d at 299.

If the wife in *Friebel* had executed a unilateral statement under section 766.59, the income in her investment account would have been classified as her individual property rather than as marital property. However, notwithstanding such classification, the income was not received by gift and would have been divisible. It therefore appears that a unilateral statement has no effect on the division of assets at dissolution.

The interrelationship between character and identity was demonstrated in *Brandt* and *Weberg*, discussed in section 11.14, *supra*. In both cases, the court determined that the nondivisible funds deposited by one spouse in a joint account held by both spouses had not changed character. In each case, no gift was intended by the deposit in a joint account; hence, there was no change in character. However, in *Brandt*, the nondivisible funds had been commingled with divisible funds. While commingling does not necessarily make tracing impossible, in this case deposits and withdrawals were so numerous that it was impossible to tell which funds were divisible and which were nondivisible, resulting in the entire account being divisible. *Brandt*, 145 Wis. 2d at 412–13. In *Weberg*, however, only withdrawals were made, and no divisible funds

were deposited. Therefore, the remaining funds retained their identity. *Weberg*, 158 Wis. 2d at 550.

*Fowler*, discussed in section 11.14, *supra*, also demonstrated the interrelationship between character and identity. In *Fowler*, the court found that no change in character resulted from an exchange of inherited AT&T stock for shares of various other companies established when AT&T was required to divest itself of assets. The court also found that the shares' identity was preserved because they were traceable to the original nondivisible stock. *Fowler*, 158 Wis. 2d at 516. However, cash gifts that were deposited in the parties' joint bank account along with divisible funds had been so commingled as to lose their character. Unlike in *Brandt* and *Weberg*, the spouse receiving the cash gifts had not intended that they be kept separate, thus making establishment of identity unnecessary. *Id.* at 517–18.

The court's criteria in the divorce context for dividing the increase in value of a nondivisible asset caused by the labor of the nonowning spouse can be contrasted with the property law approach used by a probate court following the death of one of the spouses in *Estate of Kobylski*, 178 Wis. 2d 158. During the marriage, the spouses used marital property funds to improve and maintain a house owned by the wife (the decedent spouse) as her nonmarital property. The surviving spouse sought reimbursement of these funds from the estate since he would benefit from the estate's reimbursement of marital property. *Id.* at 166. In addition, he had made a deferred marital property election and augmented deferred marital property election under sections 861.02 and 861.03. The circuit court had found that the house was reclassified as marital property because mixing occurred by the expenditure of marital property funds and labor and because tracing was impossible. *See id.* at 167. The court of appeals reversed, noting that the surviving spouse kept meticulous records of expenditures made on the house, thus satisfying his burden of proving that the house had become mixed property as a result of these expenditures. *Id.* at 175. The estate had the burden of tracing the nonmarital component, and this burden was satisfied by reference to the surviving husband's records. *Id.* at 176. The court of appeals remanded the case to the circuit court to determine the house's enhanced value, if any, attributable to these expenditures. The court of appeals also held that the measure of reimbursement was a portion of the increased value, not the cost of improvements. *Id.* at 180.

The surviving spouse had also argued that his labor created a marital property interest in the house. To satisfy his burden of proof on the creation of marital property by labor, the surviving spouse must show substantial labor, no reasonable compensation, and substantial appreciation. *Id.* at 182–84. This is a higher level of contribution than the nonowning spouse needed to prove in *Haldemann* to be entitled to an interest in the asset by property division. The court of appeals also directed the circuit court to determine on remand whether the surviving spouse’s labor created marital property. *Id.* at 187.

## **5. Increase in Value of Nondivisible Property**

### **[§ 11.16]**

Under ordinary circumstances, a spouse’s property is not subject to division if it was acquired by inheritance or gift or was purchased with funds so acquired. Wis. Stat. § 767.61(2)(a). Also, the owner spouse must be able to show that the asset has retained its nondivisible character and its identity. An increase in an asset’s value that is not income from the asset and that is attributable to economic conditions unrelated to the efforts of a spouse is likewise nondivisible in character. *Spindler*, 207 Wis. 2d at 339–40; *Schwegler*, 142 Wis. 2d 362. For a discussion of divisibility of income from a nondivisible asset, see section 11.17, *infra*.

An increase in the value of nondivisible property attributable to the efforts of either spouse is divisible at dissolution. If the nondivisible component has retained its character and identity, these efforts result in a divisible component in the asset’s value at the time of dissolution. Situations in which the nonowning spouse’s efforts caused an increase in the value of the other spouse’s nondivisible asset were addressed in *Haldemann v. Haldemann*, 145 Wis. 2d 296, 426 N.W.2d 107 (Ct. App. 1988), and *Plachta v. Plachta*, 118 Wis. 2d 329, 348 N.W.2d 193 (Ct. App. 1984). In *Plachta*, the wife had received a house as a gift. During the marriage, the house’s value increased from \$6,000 to \$27,500. The court did not award any of the value of the house to the husband because he failed to prove that any of the increase in value resulted from his efforts. However, the court explained that failure to divide property when the nonowning spouse’s efforts contributed to that increase would cause hardship. *Plachta*, 118 Wis. 2d at 334. Thus, the appreciation in an asset not otherwise subject to division would have been divisible if the nonowning spouse’s efforts had contributed to the appreciation. De

minimis efforts will not cause the asset to become divisible. *See Spindler*, 207 Wis. 2d 327.

The issue of the effect of a nonowning spouse's efforts in improving the other spouse's nondivisible property was further developed in *Haldemann*. The wife had inherited a farm from her first husband. During the wife's second marriage, her husband worked on the farm raising hogs and made improvements on the property. The parties kept a joint bank account in which income from the hog operation was deposited and from which general farm expenses were paid. Both worked in and benefited from the hog operation. The farm's value increased during the marriage, even though farm prices in the area had generally decreased during the same period. When the divorce occurred, the wife argued that she should receive the entire farm, and the circuit court agreed. The court of appeals remanded the case to the circuit court to determine what portion of the increased value of the farm was caused by the husband's efforts. *Haldemann*, 145 Wis. 2d 307. Whereas the *Plachta* court had stated that failing to divide the increase in the value of one spouse's nondivisible asset would be a hardship to the other spouse whose efforts caused the increase in value, the court in *Haldemann* ruled that an increase that results from a spouse's efforts is part of the divisible estate and should be divided without any showing of hardship. *Id.* at 301. Citing *Torgerson v. Torgerson*, 128 Wis. 2d 465, 469–70 n.3, 383 N.W.2d 506 (Ct. App. 1986), the court observed that an asset may have divisible and nondivisible components. *See also Richmond v. Richmond*, 2002 WI App 25, 250 Wis. 2d 647, 640 N.W.2d 220 (remanding case for circuit court to determine whether spouse's efforts were "catalyst" for rapid appreciation in value of farm or whether market factors were cause).

If a court finds that an asset has appreciated because of the nonowning spouse's efforts to the extent that a portion of the value should be divided, it appears that the court will divide only the appreciation, not the entire asset. The *Haldemann* court stated that appreciation caused by the nonowning spouse's "unusual and uncompensated" efforts, that is, efforts beyond the usual and normal marital responsibilities, is divisible property. *Haldemann*, 145 Wis. 2d at 301–02. The court found this consistent with, but not necessarily the same as, the requirement that the appreciation be "substantial," that the labor be "substantial," or that reasonable compensation not be received, the section 766.63(2) elements for creation of a marital property component in the value of a nonmarital asset. *Id.* at 301; *see also Krejci*

v. *Krejci*, 2003 WI App 780, 266 Wis. 2d 284, 667 N.W.2d 780 (holding that appreciation of husband's inherited asset caused by efforts of both spouses was divisible and premarital agreement making such appreciation nondivisible was unenforceable).

Similarly, in *Spindler*, 207 Wis. 2d at 339–40, the court held that the wife's efforts in maintaining the husband's inherited cottage were a de minimis factor in its increase in value. She was, however, entitled to division of the marital property funds used to maintain the property.

*Schwegler v. Schwegler*, 142 Wis. 2d 362, demonstrates how an increase in value of nondivisible property resulting from the owning spouse's efforts might affect property division. The husband had received land by gift before marriage. He then built a house on this land, also before marriage. The circuit court divided the appreciation on the house that occurred after the date of the marriage. The court of appeals remanded the case for the circuit court to determine the gift component of the improved real estate—that is, how much of the value of the property was attributable to the land and how much to the house—and to then determine the source of any appreciation. Appreciation as a result of general economic factors remains nondivisible along with the gift, and appreciation as a result of efforts of the nonowning spouse becomes divisible. *Id.* at 366. The opinion does not say what should happen to appreciation caused by the owning spouse's efforts. However, because the court of appeals directed the circuit court to determine the source of any appreciation, it appears that appreciation of a nondivisible asset as a result of efforts or other contributions of either the owning or nonowning spouse may be considered in determining how the divisible component of an asset is divided. See also Martin Gales, *Expenditure of Community Labor and Assets on Separate Property in Washington*, 12 Community Prop. J. 269 (1985); Peggy L. Podell, *Enhanced Value of a Closely Held Corporation at the Time of Divorce: What Role Will Wisconsin's Marital Property Act Play?*, 69 Marq. L. Rev. 82 (1985); Brett R. Turner, *Distinguishing Between Active and Passive Appreciation in Separate Property: A Suggested Approach*, 13 Divorce Litig. 73 (2001).

An increase in the value of a nondivisible asset as a result of the efforts of the owning spouse occurred in *Lendman v. Lendman*, 157 Wis. 2d 606, 460 N.W.2d 781 (Ct. App. 1990). The husband set up a corporation with \$8,500 in inherited funds and loaned the corporation approximately \$25,000, also from inherited funds. The corporation used this money to purchase a business and incurred additional debt for the

same purpose. The corporation paid down the debt with corporate income as it was earned. At the time of the divorce, the parties stipulated and the court found that the value of the corporation had increased because of the reduction of debt. The original nondivisible character of the stock was unchanged, but because the source of the funds used to pay the note was the husband's efforts, the court found that this portion of the value was divisible. *Id.* at 610–12.

The contrast between marital property law and the law governing property division at dissolution as they concern the increase in an asset's value as a result of the spouses' labor is illustrated by *Schorer v. Schorer*, 177 Wis. 2d 387, 501 N.W.2d 916 (Ct. App. 1993). The contested asset in this case was stock in a family business that the husband had inherited from his father. Both spouses worked in the business, but apparently most of the success of the business was attributable to the husband's time and managerial skills. The parties were married in 1971, and the company was in bankruptcy in the early 1980s, so the court found that the entire value of the multimillion-dollar company at the time of divorce resulted from the spouses' efforts. Citing *Schwegler*, *Haldemann*, *Lendman*, *Wierman*, and *Plachta*, the court acknowledged that "active appreciation" as a result of spouses' efforts is subject to division and "passive appreciation" as a result of general economic conditions is not. *Id.* at 407. The husband argued that the appreciation in the business's value should be treated as passive appreciation because the marital partnership had been adequately compensated during the marriage, presumably by his salary. *Id.* at 406. If the business were being classified under chapter 766, the separate components of value would be determined in the manner that the husband argued; that is, the appreciation of the stock classified as individual property would likewise be classified as individual property unless substantial appreciation resulted from a spouse's efforts and reasonable compensation was not received. Wis. Stat. § 766.63(2). Because reasonable compensation was received, the increase in value resulting from the spouses' efforts would be classified as the husband's individual property. However, the court found that the fact that reasonable compensation was received was irrelevant to the determination of whether the business was divisible. *Schorer*, 177 Wis. 2d at 406. Without referring to chapter 766, the court stated that "[w]hatever the effect of such a proposition elsewhere, it has not been given legal status in Wisconsin." *Id.* Consequently, the court of appeals held that the business was entirely divisible, notwithstanding that it would be classified as the husband's individual property.

In *Ayres v. Ayres*, 230 Wis. 2d 431, 602 N.W.2d 132 (Ct. App. 1999), family members gave the husband shares of a closely held corporation, which he sold shortly before the divorce. The court held that part of the value the husband received consisted of retained earnings and an increase in value attributable to general economic conditions. The court assigned this amount to the husband. The proceeds were attributable in part to undistributed dividends, which the court deemed separate from the nondivisible asset and subject to division.

The distinction between a finding that a portion of the value of a nondivisible asset is divisible and a finding that hardship exists is important. If a portion of the asset (e.g., the amount of an increase in the asset's value) is found to be divisible, the presumption of equal division of divisible assets may result in an equal division of the entire increase in value. However, if a portion of the increase in value of the nondivisible asset is divided because of hardship, the court should divide only the amount necessary to avoid the hardship. The latter amount may be less than would be received by the nonowning spouse if the court divided the entire increase in value. *See also Wright v. Wright*, 2008 WI App 21, 307 Wis. 2d 156, 747 N.W.2d 690 (holding that insurance proceeds paid to and retained by nondivisible corporation to replace destroyed assets remained nondivisible).

Since the general rule is that all property of the spouses is divisible, the burden of proving that an asset is nondivisible is on the spouse attempting to exclude it from division. *Steinmann*, 2008 WI 43, ¶ 26, 309 Wis. 2d 29; *Brandt*, 145 Wis. 2d at 408. That spouse must show that the character of the property has not changed, so that it continues to be nondivisible, and that the property can be identified and traced. *Preuss v. Preuss*, 195 Wis. 2d 95, 536 N.W.2d 101 (Ct. App. 1995); *Brandt*, 145 Wis. 2d at 408. If the owning spouse meets that burden, the nonowning spouse attempting to include all or a portion of the increase in value as a divisible asset then has the burden of proof as to how the increase became divisible and how the divisible component should be valued. *Spindler*, 207 Wis. 2d at 338–39; *Brandt*, 145 Wis. 2d at 409; *see also* William A. Reppy, *Calculating the Spousal Interests in “Mixed” Property Cases Under Wisconsin’s Marital Property Act*, 7 Wis. Law. Marital Prop. F. 17 (1990). The concepts of character and identity are discussed at sections 11.14–.15, *supra*.



## 6. Income Generated by Nondivisible Property

### [§ 11.17]

Income from a marital property asset is classified as marital property. Wis. Stat. § 766.31(4). Income from a nonmarital property asset (i.e., individual property and predetermination date property) is also classified as marital property unless a unilateral statement relating to the income is executed under section 766.59. *Id.*; *see also* Wis. Stat. § 766.31(7p). Income from any asset can also be reclassified by gift or by marital property agreement. *See supra* § 2.5 (regarding how property can be reclassified).

In a case decided before the marital property laws became effective, the Wisconsin Court of Appeals found that the income generated by an asset that was nondivisible at divorce was nonetheless distinct from the asset itself and was subject to division. *Arneson v. Arneson*, 120 Wis. 2d 236, 355 N.W.2d 16 (Ct. App. 1984). The husband had received as a gift 100 shares of stock in a family-owned corporation. He purchased an additional 150 shares of stock in the family corporation and other unrelated securities with the dividends generated by the stock he had received as a gift. In dividing the purchased stock and other securities, the court distinguished assets purchased with income generated by a nondivisible asset from the underlying asset itself. The court characterized this income as “earned,” rather than acquired by a spouse through gift or inheritance, which removed the income from the category of assets not subject to property division. *Id.* at 244–45. Therefore, the stock and other securities purchased with dividends generated by the husband’s nondivisible stock were subject to division.

Similarly, in a case decided after the marital property laws became effective, the court in *Friebel v. Friebel*, 181 Wis. 2d 285, 510 N.W.2d 767 (Ct. App. 1993), held that income generated by the wife’s nondivisible assets was divisible. This income did not include income earned before distribution by assets held in a trust established by the wife’s father; the divisible income was that earned on an investment account in which the wife had deposited her trust distributions. Discretionary distributions of income or principal of a trust were gifts by the settlor when distributed and were nondivisible. *See supra* § 11.14.

The court of appeals made a similar finding with respect to retained income in *Lendman v. Lendman*, 157 Wis. 2d 606, 460 N.W.2d 781 (Ct.

App. 1990). The husband used inherited funds to set up a corporation and purchase a business. The corporation took out a loan for a portion of the purchase price and paid back the loan out of its earnings. The corporation's earnings were attributable to the husband's labor, but instead of being distributed as salary, they were retained in the corporation and used to pay back the loan. The court determined that the increase in the corporation's value, stipulated by the parties to be the amount attributable to loan payments, was divisible. *Id.* at 612. This case actually involved appreciation of an asset rather than income derived from the asset because no dividend distribution was made, but the court went beyond the form of the entity and divided the value created by a spouse's efforts. *See supra* §§ 2.51, 3.42. The court did not entirely disregard the entity, however; when the court addressed maintenance, it upheld the circuit court's finding that some of the retained income might be considered in arriving at an income figure on which to base the amount of maintenance. *Lendman*, 157 Wis. 2d at 616; *see also Anderson v. Roach*, No. 2007AP1667, 2008 WL 763140 (Wis. Ct. App. Mar. 25, 2008) (unpublished opinion not citable per section 809.23(3)) (holding that income generated and retained by nondivisible partnership was divisible).

Since the decision in *Arneson*, courts have continued to make the distinction between an increase in the value of nondivisible closely held corporate stock attributable to general market conditions and an increase attributable to income earned and retained by the corporation. In *Metz v. Keener*, 215 Wis. 2d 626, 573 N.W.2d 865 (Ct. App. 1997), the court held that the retained earnings in the wife's inherited subchapter S corporation were subject to property division. The court treated these earnings as separate from the value of the corporation itself, notwithstanding that they had not been distributed by the corporation. Likewise, the court in *Ayres v. Ayres*, 230 Wis. 2d 431, 602 N.W.2d 132 (Ct. App. 1999), treated part of a corporation's retained earnings that the husband had received by gift and sold during the marriage as undistributed dividends. These were subject to division. The court found that the balance of the shares' value was attributable to general economic conditions, and it assigned this portion of the value to the husband.

Similarly, the court in *Steinmann v. Steinmann*, 2008 WI 43, 309 Wis. 2d 29, 749 N.W.2d 145, found that the fact that property can be traced to income generated by nondivisible property does not make it nondivisible.

*Id.* ¶ 43 (citing *Derr v. Derr*, 2005 WI App 63, ¶ 16, 280 Wis. 2d 681, 696 N.W.2d 170).

The wife in *Fowler v. Fowler*, 158 Wis. 2d 508, 463 N.W.2d 370 (Ct. App. 1990), had inherited stock in AT&T that the corporation exchanged for stock in different corporations established when AT&T was required to divest itself of certain assets. The court found that this transformation did not change the character of the originally inherited stock. The court held, however, that the reinvested dividends of the same stock, even stock dividends, were distinguishable from the original shares as income, and purchased stock that was traceable to those dividends was divisible.

A different result occurred in *Wierman v. Wierman*, 130 Wis. 2d 425, 387 N.W.2d 744 (1986). The wife received an interest in a real estate partnership managed by her father. Except for amounts necessary to pay income taxes, income and capital gains were retained in the partnership and reinvested. The court found the entire interest not subject to property division. The court did not address the fact that the wife's partnership account consisted in part of income from a nondivisible asset, which income would be classified as marital property. Wis. Stat. § 766.31(4). The determinative factor appears to be that the wife never received the income, and neither spouse's efforts contributed to generating the income.

Under section 766.59, a spouse may execute a unilateral statement that classifies the income from his or her nonmarital property as individual property. Wis. Stat. § 766.31(7p). Nonmarital property assets to which the statement applies may be either divisible or nondivisible at dissolution. A nonmarital property asset may be subject to division because it was acquired otherwise than by gift from a third person, before marriage, or by reason of the death of another while the spouses were married and before their determination date. Conversely, a nonmarital property asset may be nondivisible if acquired by gift from a third person, before marriage, or by reason of the death of another or with funds so acquired, provided the asset's character and identity are maintained. *See supra* §§ 11.14–15. However, *Arneson* and *Fowler* held that income attributable to nondivisible property is distinct from the asset itself and is divisible. Therefore, it appears that income from any type of nonmarital property asset is subject to division, notwithstanding that the income may be classified as individual property by a unilateral statement. *See Timothy A. Bascom, Irreconcilable Differences: Income*

*from Separate Property Under Divorce Law and Under Wisconsin's Marital Property Act*, 70 Marq. L. Rev. 41 (1986).

## **7. Deferred Employment Benefits [§ 11.18]**

Absent a marital property agreement to the contrary, deferred employment benefits earned by a spouse before or after marriage or before or after the spouses' determination date are divisible in a dissolution action. Wis. Stat. § 767.61(3) (intro.), (j). By its nature, a deferred employment benefit is not acquired by gift or inheritance. Classification as marital property or nonmarital property is immaterial. The fact that part or all of the benefits are earned before marriage is a factor that may affect how the benefits are divided because benefits attributable to premarriage employment are in the nature of property brought to the marriage. *See* Wis. Stat. § 767.61(3)(b); *Cook v. Cook*, 208 Wis. 2d 166, 560 N.W.2d 246 (1997); *Rodak v. Rodak*, 150 Wis. 2d 624, 630, 442 N.W.2d 489 (Ct. App. 1989); *see also Mausing v. Mausing*, 146 Wis. 2d 92, 429 N.W.2d 768 (1988); *Olson v. Olson*, 148 Wis. 2d 219, 435 N.W.2d 266 (Ct. App. 1988); *Loveland v. Loveland*, 147 Wis. 2d 605, 433 N.W.2d 625 (Ct. App. 1988).

A spouse working for the same employer before and after the marriage may accumulate deferred employment benefits attributable to periods before and after the marriage, resulting in the mixing of marital property and nonmarital property. Classification of such benefits would follow the formula prescribed by section 766.62. A spouse attempting to invoke section 767.61(3)(b) to achieve an unequal distribution of such an asset should attempt to show how much of the value of the deferred employment benefit is attributable to employment before the marriage and how much is attributable to employment after the marriage.

Section 766.62(2m) provides that deferred employment benefits that are mixed property are to be valued as of the date of marital dissolution or the date of the employee spouse's death, presumably in accordance with the rules of section 766.62(2), unless an agreement or court decree provides otherwise. However, section 766.62 has no effect on property division at dissolution, since section 767.61 does not require that property division correlate with classification. Even if the court wants to value such benefits and determine how much of the value is attributable to labor expended before marriage and how much is attributable to labor expended after marriage, it appears that the rules of section 766.62 need

not be followed. See *Hokin v. Hokin*, 231 Wis. 2d 184, 605 N.W.2d 219 (Ct. App. 1999) (holding that court was not required to use “coverture fraction” found in section 766.62(2) but was not prohibited from doing so). The court can use any valuation method calculated to achieve justice. *Mausing*, 146 Wis. 2d at 97–98; *Bloomer v. Bloomer*, 84 Wis. 2d 124, 267 N.W.2d 235 (1978) (discussing methods of valuing deferred-employment-benefit plan for purposes of property division in divorce); *Ably v. Ably*, 155 Wis. 2d 286, 290, 455 N.W.2d 632 (Ct. App. 1990).

In severing the economic incidents of a marriage, a court in a dissolution action has the discretion to treat a deferred-employment-benefit plan as an income stream rather than an asset to be divided. In *Dutchin v. Dutchin*, 2004 WI App 94, 273 Wis. 2d 495, 681 N.W.2d 295, the husband’s pension was a major asset of a long marriage and was in payment status at the time of the divorce. The court refused to divide the pension but instead considered it as income for the purpose of awarding the wife maintenance. The court also refused to treat the wife’s survivorship interest in the husband’s plan as property because it was derived from the pension, which was not treated as property, and to do so would have resulted in a complicated exchange of funds. Thus, the court’s ability to arrive at an equitable economic result does not depend on the property’s classification. But see *Kelly v. Kelly*, No. 2009AP852, 2010 WL 814030 (Wis. Ct. App. Mar. 11, 2010) (publication recommended) (holding that *Steinke v. Steinke*, 126 Wis. 2d 372, 376 N.W.2d 839 (1985), required court to include monthly pension payments in property division, subject to statutory presumption of equal division).

In *Waln v. Waln*, 2005 WI App 54, 280 Wis. 2d 253, 694 N.W.2d 452, the court reiterated the principle that a pension can be considered in crafting a property division, even though the spendthrift clause in the pension plan and statute prohibited the court from dividing the husband’s Milwaukee police pension itself. Also, the court has the authority to order a party to elect payment and beneficiary options, and this power does not violate the spendthrift clause.

Finally, in *Winkler v. Winkler*, 2005 WI App 100, 282 Wis. 2d 746, 699 N.W.2d 652, the court refused to reopen a divorce judgment to award an employee’s former spouse an additional portion of the employee’s Milwaukee County pension. The increase in the pension’s value occurred as a result of a statutory change made after the divorce.

## 8. Claim for Personal Injury [§ 11.19]

Under section 766.31(7)(f), a postdetermination-date personal injury recovery by a spouse from a third party is the individual property of the injured spouse, except to the extent the recovery represents reimbursement for expenses paid with marital property funds and for income loss during the marriage. Compensation for expenses paid with marital property funds and for the loss of income that would have been marital property is marital property. *Id.* In the context of a dissolution, however, the court is not bound by marital property classification rules in dividing the award.

*Richardson v. Richardson*, 139 Wis. 2d 778, 407 N.W.2d 231 (1987), set forth the supreme court's guidelines for dividing a potential personal injury award for damages caused by a third person to a spouse. In *Richardson*, the wife had a pending personal injury claim that had not been settled or tried at the time of the divorce. The court found that the entire claim was subject to division under section 767.255 (now section 767.61). However, the court established guidelines for determining the division of personal injury claims at divorce. The circuit court should presume that the injured party is entitled to the recovery for loss of future earnings, pain and suffering, and loss of bodily function. Recovery for medical expenses and compensation for earnings lost during the marriage should be divided equally. *Richardson*, 139 Wis. 2d at 780. Although the court couched these guidelines in terms of presumptions rather than as a mandatory distribution scheme for personal injury awards, it appears that these presumptions will in most instances parallel the classification rules of section 766.31(7)(f). The noninjured spouse is entitled to any recovery for loss of consortium, since loss of consortium is a type of personal injury to the noninjured spouse. *Richardson*, 139 Wis. 2d at 780; *see also Mack v. Mack*, 108 Wis. 2d 604, 323 N.W.2d 153 (Ct. App. 1982) (holding, in case decided before *Richardson* guidelines were established, that personal injury award was divisible).

The court applied these presumptions to determine the division of a structured personal injury settlement in *Krebs v. Krebs*, 148 Wis. 2d 51, 435 N.W.2d 240 (1989). While a divorce court may still divide a personal injury award equitably if circumstances warrant, the supreme court concluded that the *Richardson* presumption supersedes the section 767.255(3) (now section 767.61(3)) presumption of equal division with respect to an injured spouse's entitlement to future payments under a personal injury award. *See also Schwegler*, 142 Wis. 2d at 369 (court

remanded case for circuit court to divide wife's personal injury award according to presumptions established by *Richardson*).

The *Richardson* rule applies to personal injury awards and similar compensation that have already been received as well as those that are pending or not yet determined. The court of appeals in *Weberg v. Weberg*, 158 Wis. 2d 540, 463 N.W.2d 382 (Ct. App. 1990), held that a worker's compensation settlement received several years before the divorce should be divided pursuant to the *Richardson* criteria. The funds were subjected to a character-and-identity analysis to determine whether they continued to be nondivisible after receipt. They had been kept in a joint account, but the circuit court found that this was done only to protect the wife if the husband died and that there was no present donative intent. There were occasional withdrawals to pay debts, but the funds were not commingled with other funds. The court found that the funds' character was not changed, and that because the settlement was the sole source of the funds in the account, identity was established. As in *Popp v. Popp*, 146 Wis. 2d 778, 432 N.W.2d 600 (Ct. App. 1988), the court emphasized that there had been only withdrawals and that therefore the identity of the remaining funds was preserved. *See also* Donald A. Levy, *Marital Property Division of Personal Injury Proceeds*, 11 Wis. J. Fam. L. 85 (1991).

## **9. Income Tax Considerations in Property Division**

### **[§ 11.20]**

Transfers between spouses and transfers incident to dissolution are not subject to tax. I.R.C. § 1041. The basis of an asset that is transferred from one spouse to the other does not change. I.R.C. §§ 1041(b), 1015(e). However, if it is necessary to sell an asset to effectuate a property division, taxable gain may still be a consideration in the equitable determination of the division. Wis. Stat. § 767.61(3)(k).

## **10. Property Not Dealt with by Decree of Dissolution**

### **[§ 11.21]**

Upon the dissolution of a marriage, "the court shall divide the property of the parties and divest and transfer the title of any such property accordingly." Wis. Stat. § 767.61(1). Property received by

each spouse is therefore titled in the recipient's name and solely owned by that person, and the other spouse is divested of his or her interest. If a marital property asset is omitted from the decree for any reason, the spouses continue to own the property after the dissolution, but as a tenancy in common, not as marital property. Wis. Stat. § 766.75.

The purpose of retaining co-ownership of marital property assets not divided by the decree is to protect both spouses' interests until disposition of the property. For example, after the death of the former spouse having control of the omitted property, the other spouse might come forward to assert an ownership interest in the previously undiscovered property.

Nevada law, like Wisconsin law, provides that former spouses hold undivided assets as tenants in common. In *Williams v. Waldman*, 836 P.2d 614, 619 (Nev. 1992), the husband had acted as attorney for both parties but the settlement agreement did not include his law practice. Much later, the wife learned that the law practice was community property and was subject to division at divorce under Nevada law. The court held that because the husband had acted as attorney for the wife, he had breached his fiduciary duty of fair disclosure of financial information concerning the practice. Therefore, the asset was deemed undivided, and the wife had a right to an independent action to divide this remaining asset. See also Cal. Fam. Code Ann. § 2556 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot) (similar rule).

If undivided assets were deliberately concealed, the former spouse who did not conceal the assets may have an independent action to recover a share of those assets and may have a right to punitive damages if egregious circumstances exist. See Brett R. Turner, *Common-Law Fraud as a Remedy for Asset-Related Misconduct*, 7 Divorce Litig. 205 (1995).

Washington also has a rule similar to section 766.75. See Harry Cross, *The Community Property Law in Washington (Revised 1985)*, 61 Wash. L. Rev. 13 (1986). However, there are situations described in Washington case law in which equitable considerations have been applied to prevent a former spouse from enforcing an ownership interest in former community property omitted from a judgment of dissolution. In *Witzel v. Tena*, 295 P.2d 1115 (Wash. 1956), the wife had claimed in



the divorce in 1939 that the parties had no community property, and she made no claim to any such property. In 1953, she asserted a claim to one-half of certain substantially appreciated real estate owned by the husband that had been omitted from the divorce decree. The court found the necessary elements of equitable estoppel to bar the claim. The court held that the former wife's actions at the time of the divorce were inconsistent with the later claim, and that the former husband had relied on her earlier assertion that she made no community property claim to his property when he entered an appearance and consented to the decree. Finally, the court said that it would have been unjust to allow the former wife to benefit by the former husband's efforts in the years after the divorce.

A similar situation occurred in *Dean v. National Bank of Washington*, 360 P.2d 150 (Wash. 1961). In that case, the former husband had owned several paint stores to which the former wife asserted a claim after the former husband died. The stores' existence was not concealed at the time of the divorce, and although no value was assigned to them, sufficient information was available to allow the former wife to discover any value. For 27 years, the former wife had not challenged the former husband's ownership, and he invested considerable assets in the stores, to the point that they constituted a substantial portion of his estate. The court found all the elements of equitable estoppel and denied the wife's recovery of an ownership interest in the stores.

### **C. Relation to Interspousal Remedies [§ 11.22]**

The only significant change in chapter 767 made by the Act is found in section 767.331, titled "Actions for Certain Interspousal Remedies," which provides:

If a spouse has begun an action against the other spouse under s. 766.70 and either or both spouses subsequently bring an action under this chapter for divorce, annulment or legal separation, the actions may be consolidated by the court exercising jurisdiction under this chapter. If the actions are consolidated, to the extent the procedural and substantive requirements of this chapter conflict with the requirements under s. 766.70, this chapter controls. No action under s. 766.70 may be brought by a spouse against the other spouse while an action for divorce, annulment or legal separation is pending under this chapter.

*See supra* ch. 8. The court of appeals held constitutional section 767.331 (then numbered as section 767.05(7)) in *Haack v. Haack*, 149 Wis. 2d 243, 440 N.W.2d 794 (Ct. App. 1989). Since an action based on an interspousal remedy may not be commenced against a spouse once a divorce is pending, an interspousal action against the other spouse must be brought before filing a divorce. *Gardner v. Gardner*, 175 Wis. 2d 420, 499 N.W.2d 266 (Ct. App. 1993) (holding that matters involving spouses' property are dealt with in divorce action, and separate action for damage to marital property is barred after divorce action is commenced). *But see Knafelc v. Dain Bosworth, Inc.*, 224 Wis. 2d 346, 591 N.W.2d 611 (Ct. App. 1999) (holding that action against spouse for securities violations could be maintained after dissolution action filed). An action under section 766.70 may be brought against a third party after commencement of a dissolution action between the spouses.

If a spouse has a cause of action against the other spouse under section 766.70, and a dissolution action is dismissed or terminated, the action under section 766.70 may be commenced. In *Socha v. Socha*, 204 Wis. 2d 474, 555 N.W.2d 152 (Ct. App. 1996), the husband changed the beneficiary designation on a marital property life insurance policy to the parties' son. The change violated temporary orders entered in the dissolution action requiring that the wife remain the beneficiary. The dissolution action terminated before judgment because the husband died. The circuit court imposed a constructive trust on the proceeds of the policy, but the court of appeals remanded for a determination of the wife's and son's rights under section 766.70(6). Because the legislature had passed comprehensive statutes dealing with this situation, the court held that section 766.70(6) was the wife's sole remedy.

The remedies available under section 766.70 and chapter 767 are different and do not conflict. An action based on an interspousal remedy applies only until the marriage is dissolved, and the divorce decree applies after the dissolution. Therefore, commencing an interspousal action before commencing a dissolution action may be appropriate to provide relief for a spouse until the dissolution is final.

Certain interspousal actions would probably not be necessary to protect an aggrieved spouse's rights in marital property assets if a divorce is imminent. These include: actions alleging breach of the good-faith duty, Wis. Stat. § 766.70(1); actions for an accounting for marital property, Wis. Stat. § 766.70(2); actions for reimbursement for other than family-purpose debts paid with marital property funds, Wis.

Stat. § 766.70(5); and actions for recovery of gifts in excess of limits, Wis. Stat. § 766.70(6)(a). In cases in which one of these remedies would be appropriate against the other spouse, marital property funds typically have been disposed of by the defendant spouse, but recovery from that spouse (as opposed to a third-party transferee) is feasible as part of the property division when there are sufficient assets to compensate the aggrieved spouse. An accounting for marital property funds managed by the other spouse may also be effected as part of the dissolution proceeding. If full relief is available under divorce law and there are sufficient assets to compensate the aggrieved spouse, a separate interspousal proceeding is unnecessary. Brett R. Turner, *Here Today, Gone Tomorrow: Identification and Division of Dissipated Marital Assets*, 3 Equitable Distribution Alert 7 (Oct. 1991).

Section 767.117(1)(b) prohibits either spouse from “encumbering, concealing, damaging, destroying, transferring, or otherwise disposing of property owned by either or both of the parties” during the pendency of a dissolution proceeding without the consent of the other spouse or by order of the court or circuit court commissioner, except in the ordinary course of business, for necessities of life, or to pay reasonable costs and expenses of the action, including attorney fees. This appears to be a codification of customary existing pretrial practice. Presumably, a violation of this statute could be taken into consideration when dividing the parties’ property. *See Anstutz v. Anstutz*, 112 Wis. 2d 10, 12–13, 331 N.W.2d 844 (Ct. App. 1983) (holding that party’s squandering of assets may affect property division, causing party responsible for dissipating assets to receive lesser share). *But see Hauge v. Hauge*, 145 Wis. 2d 600, 603–05, 427 N.W.2d 154 (Ct. App. 1988) (holding that party who makes improvident but good-faith investment decisions will not necessarily receive smaller share of divisible property, even though party’s poor judgment has resulted in loss of assets); *Ward v. Ward*, No. 94-1712, 1995 WL 521867 (Wis. Ct. App. Sept. 6, 1995) (unpublished opinion not citable per section 809.23(3)) (holding that both parties were responsible for loss in asset’s value). In that event, rules for an equitable division of the spouses’ property would be applied to compensate the aggrieved spouse, but a demonstrable right to recover under one of the interspousal remedies may be persuasive to the court in determining property division.

Section 767.63 includes in the divisible estate property valued at more than \$500 that would have been part of the divisible estate but that within one year before the commencement of the dissolution action was

transferred for inadequate consideration, wasted, given away or was otherwise unaccounted for. This provision is in addition to but does not conflict with remedies available under section 766.70(6)(a). *See also* Lee R. Russ, Annotation, *Spouse's Dissipation of Marital Assets Prior to Divorce as Factor in Divorce Court's Determination of Property Division*, 41 A.L.R.4th 416 (1985).

Remedies that would determine classification or that would reclassify property are of limited use because of the divorce court's ability under section 767.61 to award property regardless of classification. *See* Wis. Stat. § 766.70(2), (4). However, a judicial finding that a particular asset is inherited individual property should result in issue preclusion in a later dissolution proceeding involving the same asset.

The usefulness of assigning existing liabilities under section 766.70(4)(a)3. is limited, particularly since the court as part of the dissolution decree can assign liability. Wis. Stat. § 766.55(2m).

In contrast, a separate interspousal action may be essential to protect a party's interest in marital property assets that are under the other spouse's control during the pendency of the action. For example, if a nontitled spouse is concerned that bank or brokerage accounts, the funds in which are classified as marital property, may be dissipated, adding the nontitled spouse's name to the account could mean that both signatures would be required for withdrawals. Wis. Stat. §§ 766.70(2), .51(2). The order should clearly state that both signatures are necessary; this avoids confusion with joint accounts requiring only one signature. This remedy provides more protection than would a restraining order under section 767.225(1)(h), since the previously nontitled spouse has veto power over withdrawals. It is also more flexible than freezing an account by order of the court or circuit court commissioner because the parties may agree to the use of the account. It appears, however, that direct access to the other spouse's wages cannot be achieved under section 766.70. *See supra* § 8.40.

In certain unusual circumstances, limitation of management and control over a marital property asset may be necessary to protect the spouse who does not have management and control. Wis. Stat. § 766.70(4)(a)1. Also, if one of the parties has spendthrift tendencies or is otherwise likely to incur burdensome obligations, the other party may wish to obtain an order as soon as possible to assign future obligations and to classify property acquired in the future. If there is a finding of

gross mismanagement, waste, or absence, the court may order that future obligations are the responsibility of the incurring spouse and that property thereafter acquired is the individual property of the acquiring spouse. Wis. Stat. § 766.70(4)(a)4., 5. These remedies may be especially necessary if it is anticipated that the divorce will be protracted, a marital property asset such as real estate or a business will have to be sold before judgment, and the holding spouse will not or cannot manage the transaction. Limitation of management and control for business interests is available for only a sole proprietorship; it does not apply to interests in partnerships, closely held corporations, joint ventures, or professional corporations or other interests in which a third party's rights may be adversely affected. Wis. Stat. § 766.70(4)(c).

➤ **Comment.** Although section 766.70(4)(c) was not amended after the creation of chapter 183 ("Limited Liability Companies") to exclude limited liability companies from those to which this remedy does not apply, this is probably a drafting error, and such entities would also be excluded. See Wis. Stat. § 766.70(3)(aL).

The entry of an order under section 766.70 would not prevent the court from dividing an asset using the principles of section 767.61 at the conclusion of the dissolution action. Even if the interspousal action establishes that an asset is classified as individual property because it was inherited, the dissolution court might nonetheless find that failure to divide the asset would result in a hardship to the other spouse and proceed to divide the asset.

In general, creditors whose rights arose before an order is entered under section 766.70 or who had no knowledge of the order will not be adversely affected by any provisions in the order that would otherwise limit recovery on the obligation. Wis. Stat. § 766.55(4m). However, an order entered under section 766.70(4) transferring management and control of an asset to the untitled spouse will protect the property acquired by the nonobligated spouse (usually his or her wages) from recovery by a creditor for family-purpose obligations incurred by the other spouse while the action is pending, as long as the creditor has received a copy or has actual knowledge of the order before the obligation is incurred. See *supra* § 6.36; see also Wis. Stat. § 766.55(4m). The order should require each spouse to disclose the order to future creditors so that the marital property income and assets acquired by the nonincurring spouse will be protected from recovery by family-purpose creditors of the incurring spouse. See Wis. Stat.

§§ 766.55(4m), .56(2)(c). A spouse's failure to disclose the order could subject that spouse to a finding of contempt or could affect the eventual property division.

In *Covelli v. Covelli*, 2006 WI App 121, 293 Wis. 2d 707, 718 N.W.2d 260, the court held that the husband committed marital waste, justifying an award of the majority of the marital assets to the wife, by failing to pay a corporation's sales tax under the following circumstances: only the husband was active in the corporation and he alone decided how to spend its available funds, the corporation was being audited for sales taxes, the wife was unaware of tax problems, and the husband continued to supply funds for a lavish lifestyle.

In *Noble v. Noble*, 2005 WI App 227, 287 Wis. 2d 699, 706 N.W.2d 166, the wife asked the court of appeals to increase the amount of property deemed subject to division in the dissolution action and to increase the wife's share of available assets based on these added assets. The husband and his brother were members of a farming partnership. The partnership owned no real estate; the land was rented by the partnership and owned by the brothers and their wives. The disputed three parcels were owned by the husband's brother and his wife, but the husband had declined to acquire an interest when they were purchased. The partnership financed the purchase, and the value of this receivable was included in the property division, but the husband took no interest. All parties admitted the real estate was acquired in this manner to prevent the wife from acquiring an interest in case of divorce.

The court held that the marital estate was not diminished or wasted by the husband's failure to obtain an interest in the real estate. The court distinguished waste, which assumes that assets are no longer in the estate, from the failure to take advantage of an opportunity to increase the marital estate. "In short, the law does not require a party to a prospective divorce to take advantage of an opportunity to acquire property that would increase the value of the marital estate, and the use of partnership funds to finance the purchase of the properties did not improperly dissipate the value of the marital estate." *Id.* ¶ 2; *see also supra* § 8.12; Matthew J. Price, *Case Spotlight: Noble v. Noble*, 26 Wis. J. Fam. L. 24 (2006).

## D. Rights of Creditors at Dissolution [§ 11.23]

### 1. In General [§ 11.24]

One of the major objectives of the Marital Property Act was to increase nonwage-earning spouses' access to credit. *See supra* § 5.42. The Act accomplished this by expanding management and control rights in credit transactions, Wis. Stat. § 766.51(1m), and by requiring that creditors consider the property available to satisfy obligations when determining a spouse's creditworthiness. *See* Wis. Stat. §§ 766.55, .56(1). A person's marital status is an essential element in determining creditworthiness, since obligations incurred in the interest of the marriage or the family may be satisfied from all marital property assets as well as from the nonmarital property assets of the incurring spouse. Wis. Stat. § 766.55(2)(b). A potential creditor must consider most marital property assets acquired by, as well as obligations incurred by, either or both spouses. It therefore follows that creditors who rely on and extend credit based on the existence of the marriage should be protected, although they may not be if the marriage is dissolved and the property previously classified as marital property is thereafter solely owned. *See supra* ch. 5, ch. 6.

The right of creditors to recover marital property assets is unchanged by the separation of spouses or the commencement of an action for dissolution. However, after the dissolution, any income earned by the nonincurring spouse is not available to the creditor unless the decree so provides, even though the creditor may have relied on that income in granting the credit. Wis. Stat. § 766.55(2m). This result is consistent with the treatment of creditors after the incurring spouse dies, unless the obligation resulted from an extension of credit (which applies to most obligations) or is a tax obligation to the state. Wis. Stat. § 859.18(3). If the incurring spouse dies owing an obligation to a creditor who regularly extends credit or to the state of Wisconsin for a tax obligation, the surviving spouse's income is available for recovery. *Id.* For example, if one spouse incurs department-store charge-card obligations and the spouses are later divorced, unless the decree provides for payment by the nonincurring spouse, the store cannot recover from the income of the nonincurring spouse, even though the store might have considered the income of the nonincurring spouse in deciding whether to issue the charge card to the incurring spouse. *See infra* § 11.25, *supra* § 5.37. If the incurring spouse had died and the spouses were not divorced, the

store could recover from the income of the nonincurring surviving spouse. The 1985 Trailer Bill Original Nontax Note to section 766.55(2m) acknowledges the limitation on creditors' rights upon dissolution of the marriage and how these rights differ from the provisions for creditors' rights at the death of the incurring spouse. *See* Wis. Stat. Ann. § 766.55 Legis. Council Notes—1985 Act 37, §§ 90–98 (West 2009). The 1985 Trailer Bill Original Nontax Note to section 859.18 points out that these two forms of terminating a marriage are distinguishable but does not state why the treatment of creditors is different in those two circumstances. *See* Wis. Stat. Ann. § 859.18 Legis. Council Notes—1985 Act 37, § 169 (West 2002). One reason for the difference may be that only in a dissolution action can the court assign responsibility for payment of an obligation to a nonobligated or nonincurring spouse and thus protect the rights of creditors and parties on a case-by-case basis. *See* Wis. Stat. § 766.55(2m).

## **2. Assignment of Obligations by Decree of Dissolution [§ 11.25]**

The court may assign the responsibility for payment of specific debts to either the incurring or the nonincurring spouse as part of the decree, but as a nonparty to the dissolution action, a creditor is not bound to look only to the spouse to whom the debt is assigned if the other spouse is otherwise liable. Wis. Stat. § 766.55(2m). The provision in the decree making the nonincurring spouse responsible for the obligation allows the creditor to recover from either spouse as if both spouses incurred the obligation. *Id.*; *see also* Wis. Stat. § 803.045; *supra* § 6.53 (procedure to recover payment of obligations from spouses).

If an obligation incurred by one spouse in a pending divorce is substantial, a creditor may consider attempting to intervene in the dissolution action, or at least informing the spouses of the creditor's interest in the outcome, to persuade the court or the parties to assign the debt to the spouse who will be better able to pay. *See* Wis. Stat. § 803.09; *Sokaogon Gaming Enter. Corp. v. Curda-Derickson (In re Marriage of Curda-Derickson v. Derickson)*, 2003 WI App 167, 266 Wis. 2d 453, 668 N.W.2d 736 (holding that husband's restitution debt was not incurred in the interest of marriage or family; creditor had intervened in dissolution action). If the incurring spouse is the one less able to pay, it will be in that spouse's interest to ask the court to assign responsibility for obligations to the spouse better able to pay. However,



neither section 767.61 nor chapter 766 requires that the court consider the income or property relied on by a creditor when the obligation was incurred in determining the spouse to whom an obligation is assigned. *See supra* ch. 6; *see also* Catherine J. Furay, *Credit Aspects of Marital Property and Divorce*, 11 Wis. J. Fam. L. 103 (1991).

It should be noted that under section 766.55(2m), the earned or unearned income of the nonincurring spouse is unavailable to satisfy a family-purpose debt after entry of the decree unless the decree assigns responsibility to the nonincurring spouse. It appears that a creditor could recover income from the nonincurring spouse after the judgment is rendered orally in court but before it is reduced to written judgment and entered by the clerk of court. *See* Wis. Stat. § 806.06(1).

Former marital property assets received by either spouse in a decree of dissolution are available to satisfy a family-purpose obligation to the extent of the asset's value at the date of the decree. Wis. Stat. § 766.55(2m). After the judgment, any appreciation in value of an asset assigned to the nonincurring spouse would not be available.

➤ **Comment.** If the value of an asset declines, then the creditor would probably be limited to its value on the date of recovery because the nonincurring spouse need not make up for the decline with other property that would not otherwise be available to the creditor.

Categories of obligations other than those incurred in the interest of the marriage or the family under section 766.55(2)(b) are not mentioned in section 766.55(2m). It therefore appears that creditors holding these other obligations cannot reach former marital property assets received in the dissolution action by the spouse who is not also personally liable for the obligation, for example, under the doctrine of necessities. *See St. Mary's Hosp. Med. Ctr. v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 706 (Ct. App. 1994) (holding that under doctrine of necessities, nonincurring spouse was obligated spouse for medical debt, which was support debt under section 766.55(2)(a), and creditor was not limited to recovery under section 766.55(2m)). Premarriage, pre-January 1, 1986, tort, and other non-family-purpose creditors of the obligated spouse cannot reach any former marital property assets in the hands of the nonobligated spouse, unless the nonobligated spouse is made responsible for the obligation in the judgment of dissolution. *Sokaogon Gaming Enter. Corp.*, 2003 WI App 167, 266 Wis. 2d 453 (holding that former wife not obligated for former husband's embezzlement-restitution debt, classified

as a tort debt under section 766.55(2)(cm)). This appears to be true even if the assets received by the nonobligated or nonincurring spouse under the dissolution decree were former marital property assets generated by the obligated spouse. Such former marital property assets would have been available for recovery by the obligated spouse's premarriage or pre-Act creditors if the marriage had not been dissolved. *See* Wis. Stat. § 766.55(2)(c). However, section 766.55(2m) provides only for recovery of family-purpose obligations, and once the dissolution occurs, the assets awarded to the nonincurring spouse are no longer marital property available for recovery under section 766.55(2).

While the spouses are married, a creditor may recover any marital property assets held by either spouse to satisfy a family-purpose obligation. Wis. Stat. § 766.55(2)(b). It may be argued that in some instances, after the marriage is dissolved, equity requires that the creditor attempt collection from the spouse responsible for the obligation under the decree before proceeding against former marital property assets in the hands of the spouse who is not assigned responsibility. However, the statute does not so provide. Section 766.55(2m) allows the creditor to proceed "as if both spouses had incurred the obligation." *See also supra* §§ 6.51–.58 (procedure to recover payment of obligations from spouses). The existence of a provision assigning responsibility for payment of an obligation to one spouse might give the other spouse from whom collection is sought a right of contribution against the spouse obligated by the decree and the right to cross-claim against the responsible spouse in legal proceedings to collect the obligation.

### **3. Bankruptcy [§ 11.26]**

#### **a. Before Judgment of Dissolution [§ 11.27]**

If one or both of the parties contemplate filing for bankruptcy relief during the pendency of the dissolution or shortly thereafter, the effect of the bankruptcy law, title 11 of the United States Code, must be considered. *See generally supra* ch. 6. If filing by one spouse occurs before the judgment of dissolution is granted, 11 U.S.C. § 541(a)(2) states that all property of the debtor and all marital property assets (referred to as "community property" in the Bankruptcy Code), with limited exceptions, are included in the bankruptcy estate. This brings all property of the bankruptcy estate under the bankruptcy court's jurisdiction and under the management and control of the bankruptcy

trustee or debtor-in-possession. *See, e.g., Teel v. Teel (In re Teel)*, 34 B.R. 762 (B.A.P. 9th Cir. 1983) (holding that state court had jurisdiction over parties' status but bankruptcy court had exclusive jurisdiction over parties' community property); *Kapila v. Morgan (In re Morgan)*, 286 B.R. 678 (Bankr. E.D. Wis. 2002); *Swink v. Sunwest Bank (In re Fingado)*, 113 B.R. 37 (Bankr. D. N.M. 1990), *aff'd*, 995 F.2d 175 (10th Cir. 1993); *see also Murray v. Murray (In re Murray)*, 31 B.R. 499 (Bankr. E.D. Pa. 1983); *In re Abrams/Maldonado*, 12 B.R. 300 (Bankr. D.P.R. 1981) (bankruptcy court declined to take jurisdiction to grant divorce even though it had jurisdiction over parties' property); *supra* § 3.43 (creditor's right to recover from marital property component of mixed property asset). If both spouses file, their community property is effectively in both estates. *Ageton v. Cervenka (In re Ageton)*, 14 B.R. 833 (B.A.P. 9th Cir. 1981).

Assets that are owned by the spouses as marital property must be distinguished from assets that are owned by an entity that is owned by the spouses as marital property. *See supra* § 2.51. For example, if the spouses own partnership interests that are marital property, the assets owned by the partnership are not marital property. *U.S. West Fin. Servs., Inc. v. Berlin (In re Berlin)*, 151 B.R. 719, 723 (Bankr. W.D. Pa. 1993); *In re Lundell Farms*, 86 Bankr. 582, 590 (Bankr. W.D. Wis. 1988). If the partnership becomes a bankruptcy debtor, only partnership assets are affected; the spouses' other property is not.

Certain property is exempt and may be withdrawn from the bankruptcy estate. 11 U.S.C. § 522(b). Also, property that is of negligible value or burdensome to the bankruptcy estate may be abandoned by the trustee. 11 U.S.C. § 554. Once an asset is removed from the bankruptcy estate, it is no longer administered as part of the bankruptcy process and can be dealt with by the state court in a dissolution action.

An important consideration for a spouse with creditor problems is that the bankruptcy court can liquidate the parties' community property for the benefit of creditors, whereas the state court in a property division can only assign debts and liabilities to the parties. *See Mary Jo Heston, Bankruptcy and Dissolution: Prevention, Action, and Reaction*, Community Prop. J., Jan. 1987, at 10. Liquidation and distribution through the bankruptcy court might be to the advantage of a spouse who does not anticipate having sufficient income or assets after the

dissolution to pay joint obligations and who believes the other spouse will not pay the debts that are assigned to him or her.

Even though the bankruptcy court has exclusive jurisdiction over the spouses' marital property assets and the filing spouse's nonmarital property assets, the court may abstain or may keep jurisdiction over only as much property as is necessary to pay creditors if one party so requests. 28 U.S.C. § 1334(c)(2); 11 U.S.C. § 305; *see also* Alan N. Resnick & Henry J. Sommer, 5 *Collier on Bankruptcy* ¶ 541.13 (16th ed. 2009). The bankruptcy court will probably abstain to allow the state court to determine the spouses' rights in property, but actual distribution is under the bankruptcy court's jurisdiction. *See In re Palmer*, 78 B.R. 402 (Bankr. E.D.N.Y. 1987).

The filing of a bankruptcy petition results in an automatic stay of almost all proceedings against the debtor. 11 U.S.C. § 362(a). A party may request that the bankruptcy court lift the automatic stay to allow the state court to adjudicate the rights of the parties to property in the dissolution proceeding, even though the bankruptcy court will determine distribution. *Palmer*, 78 B.R. at 406; *see Kapila v. Morgan (In re Morgan)*, 286 B.R. 678 (Bankr. E.D. Wis. 2002) (holding void award of marital property homestead to wife by divorce court because property had previously passed to husband's bankruptcy estate). If the divorce court awards estate property to the nondebtor spouse, the nondebtor then has a claim in the debtor spouse's bankruptcy estate.

A debtor's spouse who co-owns an asset with the debtor's bankruptcy trustee may have the right to prevent sale of the entire asset. *See* 11 U.S.C. § 363(h). The debtor's spouse also has the right to purchase the estate's interest in co-owned property and in assets that were owned by the spouses as marital property. 11 U.S.C. § 363(i); *see infra* § 11.28.

### **b. After Judgment of Dissolution [§ 11.28]**

If the dissolution was completed and judgment was entered before a bankruptcy petition was filed and the debtor spouse has a continuing obligation to the nondebtor spouse, the nondebtor spouse may have a claim as a creditor in the debtor spouse's bankruptcy estate. In general, a claim arising in a decree of dissolution is not subject to discharge. 11 U.S.C. § 523(a)(5), (15). A property division may be subject to discharge under a Chapter 13 plan. 11 U.S.C. § 1328(a).

The bankruptcy trustee can sell an asset that the debtor spouse co-owns with another person, such as a spouse or former spouse who is a joint tenant or a tenant in common of a former marital property asset, only if partition is impracticable, if the sale of the bankruptcy estate's interest will realize significantly less than if the asset is sold as a whole, if the benefit to the estate outweighs the detriment to the co-owner, and if the asset is not used in the production of energy. 11 U.S.C. § 363(h). The debtor's spouse, who previously had a community property interest in an asset, can also purchase the asset from the bankruptcy estate, but considerations relating to the hardship of sale are not available. 11 U.S.C. § 363(i). The co-owner has a right of first refusal to purchase the property at the price that would be paid by a third party. *Id.* After the sale, the co-owner's interest in the proceeds, less pro rata costs of sale, are distributed to the co-owner. 11 U.S.C. § 363 (j).

If an asset was transferred to the debtor spouse by a decree of dissolution and the nonfiling spouse has retained a lien to secure payment of an eventual property division, there is no statutory right to purchase the property, but a properly perfected and unavoidable lien would still entitle the lienholder to payment from the proceeds. Unless the spouse who was awarded the asset by the dissolution decree owned the asset as nonmarital property during the marriage, this lien is not avoidable under 11 U.S.C. § 522(f)(1) as a judicial lien that impairs the debtor's homestead exemption. *Farrey v. Sanderfoot*, 500 U.S. 291 (1991); see also Henry J. Sommer & Margaret Dee McGarity, *Collier Family Law and the Bankruptcy Code* § 7.04 (1995).

On April 20, 2005, President George W. Bush signed into law the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), Pub. L. No. 109-8, 119 Stat. 23. Most provisions became effective for cases filed on or after October 17, 2005, but some changes, such as certain homestead-exemption provisions, were effective upon enactment. The details of this substantial and comprehensive revision of bankruptcy law are beyond the scope of this text. See *supra* ch. 6.

### **E. Treatment of Property and Obligations After Legal Separation [§ 11.29]**

Section 767.61 requires a property division in every judgment of divorce, annulment, or legal separation. Legal separations are included in all references to dissolution in the Act by virtue of the definition of

dissolution, Wis. Stat. § 766.01(7), notwithstanding that the different types of marital dissolution have different grounds for relief.

Section 766.75(4), which was part of the Marital Property Act before the 1985 Trailer Bill and which allowed the court to determine the treatment of marital property assets owned by the parties after a decree of legal separation, was repealed by the 1985 Trailer Bill. This repeal is consistent with section 767.61, which requires property division at dissolution. Further, the definition of *during marriage* in section 766.01(8) refers to a period in which both spouses are domiciled in Wisconsin that begins at the determination date and ends at the death of a spouse or a decree of dissolution. *See also* Wis. Stat. § 766.01(5) (*determination date* defined). The provision that income acquired during marriage is marital property unless otherwise provided, Wis. Stat. § 766.31(4), also supports the conclusion that former spouses do not own or generate marital property assets after a legal separation. *But see* Marjorie H. Schuett, *Are There Spousal Rights Under the Probate Code After a Legal Separation?* 16 Wis. J. Fam. L. 53 (1996).

### **III. Support [§ 11.30]**

#### **A. Equal Responsibility for Support [§ 11.31]**

Each spouse has an equal obligation to support the other, and each parent has an equal obligation to support minor children as provided in chapter 48 (the Children's Code) and chapter 938 (the Juvenile Justice Code) and according to the standards set by chapter 49 (relating to public assistance). Wis. Stat. § 49.90(1m). Each parent also has an obligation to support a child of a dependent person. Wis. Stat. § 49.90(1)(a)2., (1m).

There may be criminal sanctions for unjustified failure to support a dependent child, a grandchild, a spouse, or a former spouse. Wis. Stat. § 948.22(2); *see, e.g., State v. Monarch*, 230 Wis. 2d 542, 602 N.W.2d 179 (Ct. App. 1999); *State v. Lenz*, 230 Wis. 2d 529, 602 N.W.2d 173 (Ct. App. 1999). There are also sanctions under federal law if a child-support payor living in a different state from his or her children fails to make required payments. 18 U.S.C. § 228; *United States v. Black*, 125 F.3d 454 (7th Cir. 1997).

The intent of the legislature in regard to support obligations is stated in section 765.001(2):

Each spouse has an equal obligation in accordance with his or her ability to contribute money or services or both which are necessary for the adequate support and maintenance of his or her minor children and of the other spouse. No spouse may be presumed primarily liable for support expenses under this subsection.

The measure of support for which a spouse is responsible is determined under section 767.501, which authorizes an independent action for support. The considerations in section 767.511, relating to child support, and in section 767.56, relating to maintenance, are used to determine the support obligation at dissolution. *See* Wis. Stat. § 767.501(2)(b). Obligations arising under the duty of support may be satisfied from all marital property assets and all other property of the obligated spouse. Wis. Stat. § 766.55(2)(a).

In addition to the direct obligation to the spouse to whom the duty of support is owed, a spouse required to furnish support is directly liable to a creditor furnishing necessary goods and services to the other spouse. This is known as the *necessaries* doctrine. *See St. Mary's Hosp. Med. Ctr. v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 706 (Ct. App. 1994) (holding that obligation under doctrine of necessities is included in category of support debt under section 766.55(2)(a)). The application of this doctrine may be different from the obligation for support, since the amount due for support is determined according to factors under section 767.56. For a detailed description of the support obligation and the necessities doctrine, see sections 5.106,–.110, 6.4–.6, and 8.17, *supra*.

The federal criminal statute creating sanctions for failure to support children in a different state, 18 U.S.C. § 228, has been held partially unconstitutional by *United States v. Pillor*, 387 F. Supp. 2d 1053 (N.D. Cal. 2005), and *United States v. Morrow*, 368 F. Supp. 2d 863 (C.D. Ill. 2005). Both courts held that the mandatory presumption of willful refusal to pay support violated the defendant's due-process rights in that it impermissibly relieved the government of its burden of persuasion with respect to an element of the offense. The courts upheld the statute in all other respects.

## **B. Property Available for Recovery of Support Obligations [§ 11.32]**

An obligation to support dependents that first arises before marriage is considered a premarriage obligation, notwithstanding that periodic payments are subject to modification and continue to be due and payable after marriage. *See* Wis. Stat. § 766.55(2)(c)1.; *see also* *St. Mary's Hosp. Med. Ctr. v. Brody*, 186 Wis. 2d 100, 519 N.W.2d 706 (Ct. App. 1994) (regarding recovery of support obligations arising under necessities doctrine).

The property available to meet an obligation to support a former spouse or minor children is any property that would have been available but for the subsequent marriage. Wis. Stat. § 766.55(2)(c)1. This includes all the obligated spouse's nonmarital property assets and that part of the marital property assets that would have been the property of the obligated spouse if he or she had not remarried or had not married for the first time, if the obligation involves minor children born before any marriage. *Id.* All marital property assets generated by the obligated spouse are available notwithstanding the current spouse's ownership interest in the assets. The purpose behind this provision is to prevent the obligated spouse's subsequent marriage from diminishing or increasing the assets available to a minor child or former spouse for support. Consistent with this purpose, marital property assets that would have been the solely owned property of the subsequent spouse but for the marriage are not available, even though the obligated spouse has a one-half interest in the assets. Wis. Stat. § 766.55(2)(c)1. For example, the nonobligated spouse's wages cannot be garnished to meet the obligated spouse's support obligation, even though the obligated spouse has a one-half interest in such wages. If the wages of both the obligated spouse and the nonobligated spouse are commingled in a joint bank account or other marital property asset, it is not clear how the payee's right to recover is affected. *See supra* § 6.24. The resolution of this issue may depend on who has the burden of proof for tracing the assets. *See supra* ch. 3..

It is important to note that title is not a factor in determining which assets are available to meet support obligations. Therefore, if a spouse is obligated to support a former spouse or children born before the current marriage, and the obligated spouse who has married or remarried uses his or her wages to purchase a car titled in the name of a new spouse, then



(unless the car was a gift that is not avoidable as a fraudulent conveyance and intended to be the individual property of the new spouse) the car could be recovered to satisfy the support obligations. Wis. Stat. § 766.31(10). Under the rule of section 766.55(2)(c)1., absent a gift, the car is classified as marital property, notwithstanding title, and it would have been the property of the obligated spouse but for the marriage. Therefore, it can be recovered for support of the former spouse or minor children.

Frequently, marital property funds are used for the support of a previous spouse or for minor children not of the current marriage. These obligations are treated as premarital obligations under section 766.55(2)(c)1. The nonobligated spouse may have a right to recover from the obligated spouse marital property funds equal in value to the amounts so used. Wis. Stat. § 766.70(5). The recovery would be the individual property of the nonobligated spouse. Wis. Stat. § 766.70(5). This right of reimbursement is affected by the rights of any third parties and by equitable considerations. Wis. Stat. § 766.70(5). It may be appropriate to reserve this remedy for cases in which the obligated spouse has acted in bad faith, for example, by using marital property funds to make payments despite having substantial nonmarital property funds available.

### **C. Maintenance [§ 11.33]**

The obligation to support a spouse often extends beyond the dissolution of the marriage in the form of maintenance. Wis. Stat. § 767.56. Although the remarriage of the payee terminates the obligation on application of the payor, Wis. Stat. § 767.59(3), the remarriage of the payor does not. As to the subsequent marriage of the payor, the maintenance obligation to the payor's former spouse is a premarriage obligation that is collectible pursuant to section 766.55(2)(c)1.

The Wisconsin Supreme Court addressed the effect of marital property law on the income earned on assets owned by a maintenance payor's subsequent spouse in *Poindexter v. Poindexter*, 142 Wis. 2d 517, 419 N.W.2d 223 (1988). The maintenance awarded to the payor's previous spouse was based on a percentage of the payor's income. Divorced in 1980, the payor remarried in 1981, before the passage of the Marital Property Act. In 1985, the circuit court found that changes in the payor's circumstances warranted modification of the maintenance

amount. Some of the changes, however, resulted from the payor's transfer of certain assets, including income-producing real estate, to his second wife, also before the effective date of the Marital Property Act. Although the circuit court had concluded that the income from the transferred properties should be entirely included in the maintenance calculation, the court of appeals held that only one-half the income should be included.

The supreme court affirmed the circuit court's use of a percentage-of-income standard to set the amount of maintenance for the first wife. *Id.* at 529–37. The court discussed the classification of income from assets transferred to the second spouse and concluded that the income should be excluded from the maintenance calculation, on the ground that the parcels of real estate were the second wife's predetermination date property and should have been treated as if they were her individual property assets. *See id.* at 541; *see also* Wis. Stat. § 766.31(9). Section 766.31(4) classifies income from such assets as marital property. However, a predetermination date obligation, as the husband's maintenance obligation was determined to be, may be satisfied only from the payor's nonmarital property assets and from marital property assets that would have been available for the payor's obligations but for the Act. Wis. Stat. § 766.55(2)(c)2. These assets, and the income from them, would have belonged solely to the second wife but for the Act. The supreme court remanded the case for the circuit court to consider the maintenance amount, since it may have been based on the circuit court's erroneous assumption that the rental income could be reached to enforce collection. *Poindexter*, 142 Wis. 2d at 543–44. The court also stated that section 766.55(2)(c)1. (premarriage obligations) did not apply in this case because the prior marriage and divorce occurred before the Marital Property Act was enacted, thereby making this a pre-Act rather than a premarriage obligation. *Id.* at 542.

The court did not discuss the effect of section 766.31(10), relating to interspousal gifts and the income from such gifts, although it is arguable that the section does not apply to interspousal predetermination date gifts. *See supra* § 2.94. If the interspousal-gift rule of section 766.31(10) had applied, the income from the transferred assets would not have been classified as marital property, and the result would have been the same, albeit based on a different reason.

In *Guzikowski v. Kuehl*, 153 Wis. 2d 227, 451 N.W.2d 145 (Ct. App. 1989), the court of appeals awarded the former wife attorney fees, a form

of maintenance, on her cross-appeal that resulted in an increase in child support payable to her by her former husband. The fees were incurred after the former wife had remarried. Even though the wife owned one-half of her new husband's income, the court determined that it did not have to ignore the fact that the new husband, and not the wife, was the source of that income. The court concluded that it could disregard the new husband's income in awarding the attorney fees to the wife if considering the new husband's income would only burden his efforts with the cost of an unrelated party's legal proceedings—namely, the dispute between the former spouses.

#### **D. Setting Amount of Child Support Obligations Arising Before Current Marriage [§ 11.34]**

In setting child support to be paid to the parent having custody or primary placement by either the noncustodial parent or the parent having joint custody but not having physical placement of a minor child, the court is required to set the amount as a percentage of the payor parent's gross income from all sources (after deducting business expenses but before deducting taxes and Social Security contributions, *see* Wis. Admin. Code § DCF 150.02(13)), plus imputed income in some circumstances, unless it would be unfair to the child or any of the parties to do so. Wis. Stat. § 767.511(1j), (1m). The rules governing the percentage-of-income standard for child support are contained in Wisconsin Administrative Code chapter DCF 150 (formerly chapter DWD 40). Child support may be set as a dollar amount or as a percentage of income. Wis. Stat. § 767.511(1)(a). If there is a finding that the application of the percentage standard would be unfair to the child or any of the parties, the court can consider a number of equitable factors under section 767.511(1m) and make appropriate findings. Wis. Stat. § 767.511(1n).

Except for some paternity-support determinations, the amount of a child-support obligation will usually be decided in the first instance at the time of the parents' divorce, that is, before the payor parent remarries. All these rules are silent on the calculation of child support according to the percentage standards when the obligated parent marries or remarries and the income used in the original calculation of support is now the marital property of the payor and a new spouse.

An obligation arising before marriage, such as an obligation to support a child not of the current marriage, may be satisfied only from the parent's nonmarital property assets and from marital property assets that would have been the property of the obligated parent but for the obligated parent's subsequent marriage. Wis. Stat. § 766.55(2)(c)1. This is the same income that would have been available to meet the support obligation if the parent had not married.

The question of the extent to which the child support payor's subsequent spouse's income is to be considered, if at all, arises when a motion is made for modification or revision of the judgment under section 767.59. Section 767.59(1c)(a)2. states that the court may "[m]ake any judgment or order on any matter that the court might have made in the original action." The statute further states, "a revision under this section of a judgment or order with respect to an amount of child or family support may be made only upon a finding of a substantial change in circumstances." Subsections (1f)(b) and (c) of section 767.59 describe events that constitute a rebuttable presumption of a substantial change of circumstances and events that may constitute such a change, respectively. The named events do not include the payor's remarriage, which might entail consideration of the payor's marital property interest in income earned by the new spouse or the new spouse's interest in marital property income earned by the payor. In the appropriate case, however, the court may consider "[a]ny other factor that the court determines is relevant." Wis. Stat. § 767.59(1f)(c)4. Section 767.59(2) provides that the percentage standards, *see* Wis. Admin. Code § DCF 150.03(1), must be applied to a modification of child support unless, on the request of a party and after consideration of the factors listed in section 767.511(1m) (relating to the totality of the child's circumstances), the court finds by the greater weight of the credible evidence that the use of the percentage standards is unfair to the child or to any of the parties. *See Burger v. Burger*, 144 Wis. 2d 514, 424 N.W.2d 691 (1988).

The effect of the payor's interest in a new spouse's income after remarriage was addressed by the Wisconsin Supreme Court in *Abitz v. Abitz*, 155 Wis. 2d 161, 455 N.W.2d 609 (1990). The circuit court had held that the amount of support to be paid by the noncustodial mother was to be calculated by adding her income and that of her current husband, dividing by two, and applying the percentage standard to the resulting amount. The support thus determined equaled 57% of the mother's gross income. The order further stated, however, that the child

support was to be paid only from the mother's nonmarital property and from her marital property that would have been her property but for the marriage. Her current husband's income would not be available to satisfy her obligation. The court of appeals had held that the current husband's income could not be used either to set the amount of support or as a source of collection, and that the totality of the circumstances should be considered, except for the current husband's marital property income. The supreme court affirmed the court of appeals' decision and remanded the case for determination of child support. However, the supreme court found that the court of appeals had erred in eliminating the earnings of the payor wife's current husband when considering the parties' total economic circumstances. The court held that if the standards are used, the percentages must be applied to the "gross income" of the obligated spouse "as if he or she were still single." *Abitz*, 155 Wis. 2d at 181–82; *see also Krieman v. Goldberg*, 214 Wis. 2d 163, 171, 571 N.W.2d 425 (Ct. App. 1997); *Miller v. Miller*, 171 Wis. 2d 131, 491 N.W.2d 104 (Ct. App. 1992).

*Abitz* was decided before subsections (2) and (2m) were added to section 767.32 (now section 767.59) by 1991 Wisconsin Act 39. Now, when modifying child support, the court must use the percentage standard unless, on the request of a party, "after considering the factors listed in s. 767.511(1m) [relating to the totality of the child's circumstances], the court finds, by the greater weight of the credible evidence, that the use of the percentage standard is unfair to the child or to any of the parties." Wis. Stat. § 767.59(2)(b). Had this statutory requirement been in effect at the time *Abitz* was decided, the court would first have had to consider each parent's earning capacity and total economic circumstances to find that the percentage standard was unfair to the children or the parties. Wis. Stat. § 767.59(1), (2)(a), (2)(b). Only then could it have set support based on the parties' total economic circumstances. *See* Wis. Stat. § 767.59(2)(b).

*Abitz* also was decided before the child-support percentage-of-income standard provisions in the Wisconsin Administrative Code (now at chapter DCF 150) were revised. Section DCF 150.02(13) now defines *gross income* quite broadly but does not clearly include a new spouse's income. *Krieman*, 214 Wis. 2d 163, was decided after these revisions, but it followed *Abitz* without discussing the definition of gross income in the administrative code.

The income of an obligated parent's new spouse can be one of the considerations in setting child support, despite the fact that the obligation was a pre-Act debt. In *J.G.W. v. Outagamie County Department Of Social Services (In the Interest of A.L.W.)*, 153 Wis. 2d 412, 451 N.W.2d 416 (1990), also decided before the creation of subsections 767.32(2) and (2m) (now subsections 767.59(2)(a) and (b)) and cited in *Abitz*, before the effective date of the Act the child had received medical assistance benefits, for which the father was obligated. Wis. Stat. §§ 766.55(2)(c)2., 46.03(18), .10(3). The court held that the fact that a nonobligated spouse's income is considered in setting the amount does not impose liability on the nonobligated spouse, nor is the nonobligated spouse's income available to the creditor for satisfaction of the debt. *A.L.W.*, 153 Wis. 2d at 426.

The court in *Brad Michael L. v. Lee D. (In re Paternity of Brad Michael L.)*, 210 Wis. 2d 437, 564 N.W.2d 354 (Ct. App. 1997), addressed the issue of how the income of a married child-support payor's spouse affected the child-support obligation in a paternity action. The circuit court had added together the gross income of the obligated father and his wife, divided the result by two, and applied the percentage standard to this amount. The court of appeals held this to be error. The court stated that under *Abitz*, only the father's income, determined as if he were single, should be used to set support. In this respect, the court deviated from the definition of *gross income* in Wisconsin Administrative Code section HSS 80.02(13)(a) (now DCF 150.02(13)), that is, gross income for federal income-tax purposes. However, the father's wife's income could be considered in the payor's total economic circumstances under section 767.59(2)(b), and her income could be used to determine whether the payor was able to *satisfy* the obligation. *Id.* at 457.

In *Steven J.S. v. Steven M.S. (In re Paternity of Steven J.S.)*, 183 Wis. 2d 347, 515 N.W.2d 719 (Ct. App. 1994), the court of appeals reversed the circuit court on the ground that the circuit court improperly added the income of the payor's spouse, who worked in the payor's business, in determining the payor's gross income for the purpose of calculating child support. Furthermore, the payor's spouse was not considered a *dependent household member* as that term was used in Wisconsin Administrative Code section HSS 80.02(10) (1995) (now section DCF 150.02(9)) for the purpose of imputing her income to him. The court of appeals did not rely on or mention marital property law in any determination affecting child support. However, the court observed that

the spouse's income might be imputed to the payor if payments to the spouse were being used to divert the payor's income to reduce the amount of the payor's child support, citing *Evjen v. Evjen*, 171 Wis. 2d 677, 492 N.W.2d 361 (Ct. App. 1992). *Steven J.S.*, 183 Wis. 2d at 353; see also *Daniel R.C. v. Waukesha County (In the Interest of Kevin C.)*, 181 Wis. 2d 146, 510 N.W.2d 746 (Ct. App. 1993) (holding that spouses were manipulating assets to avoid responsibility for residential treatment for husband's child and allowing consideration of nonliable wife's income in imputing income to liable husband, notwithstanding marital property agreement classifying each spouse's assets as individual property of that spouse); *Evjen*, 171 Wis. 2d 677 (holding that court could consider payor's diversion of income to his current wife through his corporation in setting support); *Weston v. Holt*, 157 Wis. 2d 595, 603–05, 460 N.W.2d 776 (Ct. App. 1990) (holding that change in child support requires consideration of total economic circumstances); *Long v. Wasielewski*, 147 Wis. 2d 57, 432 N.W.2d 615 (Ct. App. 1988); *Hime v. Muir*, 128 Wis. 2d 293, 381 N.W.2d 607 (Ct. App. 1985). (*Hime* was decided before the Wisconsin Administrative Code Provisions dealing with child support were revised to provide for serial families.)

The court of appeals held in 1993 that a payor under an effective child-support order who later has other children was not a *serial family payer* within the meaning of Wisconsin Administrative Code section HSS 80.02, unless the child-support obligation to the subsequently born children arises pursuant to a court order. *Brown v. Brown*, 177 Wis. 2d 512, 522, 503 N.W.2d 280 (Ct. App. 1993). This interpretation is now codified in the replacement to section HSS 80.02, section DCF 150.02(25) of the Wisconsin Administrative Code, which now uses the term *serial-family parent*. See also Connie M. Chesnik, *New Child Support Guidelines Effective in 2004*, 24 Wis. J. Fam. L. 7 (2004).

The Wisconsin Supreme Court, in *Burger v. Burger*, 144 Wis. 2d 514, 424 N.W.2d 691 (1988), considered how a custodial parent's marital property interest in her new spouse's income affected the level of child support she was to receive. After the mother remarried and voluntarily quit working, she asked the court to increase child support, based on the children's father's increased income, her own lack of income, and the children's increased needs. The father asked that the mother's marital property interest in her husband's earnings be considered as her income. The family court commissioner found that there had been a substantial change in circumstances and set a new support order based solely on a percentage of the noncustodial father's income in accordance with the

percentage standards under section 767.25(1j) (now section 767.511(1j)). The circuit court affirmed this amount.

Upon certification for direct appeal, the supreme court affirmed the child support amount. The court found that it was not an abuse of discretion to find that the increase in the ages of the children constituted a substantial change of circumstances as required by section 767.32 (now section 767.59) to warrant an increase in support. *Id.* at 524. It approved the use by the family court commissioner of the percentage standards in reaching the amount of the modified support order, although section 767.32(2) (now section 767.59(2)) was not in effect and use of the percentage standard was not required. *Id.* at 519 n.1. According to the supreme court, once the family court commissioner had determined that a substantial change had occurred and that the percentage standard was appropriate to determine the modified amount of support, the amount of the custodial mother's income from any source, including her interest in her new husband's income, was irrelevant. *Id.* at 525. The court did not need to address whether a payor's or payee's marital property interest in the earnings of his or her new spouse is a factor in determining the obligation to pay or the entitlement to receive support.

Although the court stated that *Poindexter v. Poindexter*, 142 Wis. 2d 517, 419 N.W.2d 223 (1988), had answered the question of attribution of a new spouse's income, *Poindexter* did not deal with the issue before the court in *Burger*. The mother's income in *Burger* was not a consideration in setting the modified support order under the percentage standards, and she was the only party who had remarried. *Poindexter* would not have provided guidance for the situation in *Burger* if the commissioner had elected not to apply the percentage standards but to consider the resources of the custodial parent, because *Poindexter* does not indicate whether the earnings of a parent's new spouse would enter into the equation and, if so, how. *See supra* § 11.33.

A marital property agreement cannot adversely affect the right of a child to support. Wis. Stat. § 766.58(2). The spouses in *Ondrasek v. Tenneson*, 158 Wis. 2d 690, 462 N.W.2d 915 (Ct. App. 1990), had entered into an agreement incident to their divorce that prohibited the wife from requesting child support as long as she was receiving periodic payments. The court found that an agreement that purported to prevent the court from taking the children's needs into consideration was against public policy. Conversely, an agreement that prohibited a court from taking the payor's reduced income into consideration in setting support



was also against public policy. *Krieman*, 214 Wis. 2d at 176–78; *see also Motte v. Motte*, 2007 WI App 111, 300 Wis. 2d 621, 731 N.W.2d 294 (holding that stipulation to make future payments nonmodifiable if child’s residence changed was against public policy but stipulation to forgive arrearage was not); *Wood v. Propeck*, 2007 WI App 24, 299 Wis. 2d 470, 728 N.W.2d 757 (holding that stipulation to modify child support only in event of “catastrophic circumstances” was against public policy).

A marital property agreement entered into by a noncustodial parent obligated to pay support and his or her nonobligated spouse, or a unilateral statement executed by the parent’s spouse, may not adversely affect a child’s right to support. Wis. Stat. §§ 766.58(2), .59(5). The nonobligated spouse’s income might still be a consideration in determining the amount of the parent’s obligation of support, even if the parties to the agreement opt out of the application of marital property rules. Nevertheless, the nonobligated spouse’s income would only be used in setting the level of support; it would not be recoverable to pay such support. Wis. Stat. § 766.55(2)(c)1.

A child-support order arising during the marriage, for a child born during the marriage who is the child of one but not both spouses, may also be based on considerations of the parent’s income and the parent’s spouse’s income. Because this obligation arose during the marriage, but is not likely to be considered in the interest of the marriage or the family, the obligation may be satisfied from the obligated spouse’s nonmarital property and that spouse’s interest in marital property, in that order. Wis. Stat. § 766.55(2)(d). Thus, the payee can collect from the wages of both the parent and the spouse who is not the parent of the child but only to the extent of the obligated parent’s one-half interest.

An award of child-support payments may include a requirement that the payor maintain life insurance on his or her life with the minor children as irrevocable beneficiaries as long as one of them is entitled to support. If the insured names another beneficiary and then dies, the beneficiary holds the proceeds in constructive trust for the rightful recipients. *Richards v. Richards*, 58 Wis. 2d 290, 206 N.W.2d 134 (1973). In *Duhamel v. Duhamel*, 154 Wis. 2d 258, 453 N.W.2d 149 (Ct. App. 1989), the surviving spouse was named as the beneficiary of an insurance policy with respect to which the deceased husband had been required to name as beneficiaries his children from a prior marriage. The court found that the spouse was the constructive trustee of the proceeds for the children and rejected her argument that the Marital Property Act

superseded the law of constructive trusts. *Id.* at 268–69. *See also* *Pluemer v. Pluemer*, 2009 WI App 170, 322 Wis. 2d 138, 776 N.W.2d 261 (remanding to circuit court to determine if surviving spouse was bona fide purchaser of insurance proceeds; court distinguished *Richards* and *Duhamel*). Section 766.95 states that unless they are displaced by chapter 766, the principles of law and equity supplement the chapter’s provisions. The law of constructive trusts still applies, even in instances when chapter 766 does also.

### **E. Income Tax Considerations [§ 11.35]**

Marital property classification (community property ownership under the Internal Revenue Code) has an effect on the reporting and collection of tax on income received during the marriage. Under marital property classification rules, each spouse owns a one-half interest in income classified as marital property. Wis. Stat. § 766.31(3), (4). As a result, a spouse filing a separate federal or state income tax return, or a single person who was married for part of the year, must report and is taxed on one-half the spouses’ entire marital property income. *See supra* § 9.6. Likewise, each spouse may claim one-half the deductions and amounts withheld relating to the production of marital property income. *Id.*

For Wisconsin income tax purposes, section 71.64(1)(c) provides that withholding from marital property income is to be allocated in the same manner that the income itself is or would be allocated. Marital property agreements may affect tax reporting and should be considered in the spouses’ tax planning during the pendency of a dissolution action. *See supra* § 9.52.

A potential problem arises when a divorce is pending and the earnings or other marital property income generated by one spouse, plus temporary maintenance ordered by the court under section 767.225(1)(d) to be paid to that spouse, are less than one-half the spouses’ entire marital property income that the spouse will need to report if the spouses file separate returns. This and other tax consequences can be considered by the court in awarding property division or maintenance. Wis. Stat. §§ 767.61(3)(k), .56(7).

Unless they have entered into an agreement reclassifying income as individual property before the beginning of the tax year, spouses must each report one-half their marital property income earned during the

portion of the year before the judgment of dissolution is granted. Income earned after the judgment is granted is solely owned by the party who earned it and is entirely reportable by that spouse. The spouses may want to treat their marital property income as if it were solely owned by the party receiving the income as of the beginning of the year of the divorce, because they will file as single taxpayers for that year. However, a marital property agreement is ineffective for tax purposes to retroactively reclassify income, although such an agreement is effective prospectively. *See supra* §§ 7.14, 9.52.

If the effect of a temporary maintenance order is to equalize total marital property income between the parties or if the temporary order or the final judgment provides that the spouse receiving more than one-half of the spouses' marital property income will pay any increased taxes of the spouse receiving less than half, then any inequity resulting from state or federal reporting rules should be resolved. *But see supra* § 8.40 (discussion of the lack of authority of the circuit court commissioner to divide property). *See generally supra* §§ 6.14–.17 (tax liability and classifications of property from which taxes can be collected).

Finally, section 767.61(3)(k) allows the court to consider the tax consequences of the property division in dividing property. The court should likewise be able to consider tax consequences of the separation. *See also supra* §§ 6.14–.17 (concerning the collection of taxes from the income of spouses).

## **IV. Marital Property Agreements [§ 11.36]**

### **A. Standards for Enforceability Generally [§ 11.37]**

Agreements between spouses made before or during a marriage that provide for property division and spousal support in the event of the dissolution of the marriage were given statutory recognition in 1977 Wisconsin Law ch. 105, the Divorce Reform Act, which became effective on February 1, 1978. Previously, agreements limiting a spouse's liability in the event of divorce had been found to be against public policy. *Fricke v. Fricke*, 257 Wis. 124, 42 N.W.2d 500 (1950).

Marital property agreements as defined in sections 766.58 and 766.585 are enforceable generally unless the spouse against whom enforcement is sought proves any of the following: (1) the agreement

was unconscionable when made; (2) the spouse did not execute it voluntarily; or (3) the spouse did not receive fair and reasonable disclosure under the circumstances and did not have notice of the other spouse's property and financial obligations. Wis. Stat. § 766.58(6); *see, e.g., Gardner v. Gardner*, 190 Wis. 2d 216, 232–33, 527 N.W.2d 701 (Ct. App. 1994) (holding that disclosure of stock's book value without appraisal was adequate since wife was advised of meaning of value and advised not to sign the agreement). A distinction must be made between agreements entered into in settlement of a pending divorce and agreements entered into in contemplation of an ongoing marriage. An agreement entered into when an action for dissolution is not pending is presumed enforceable under section 767.61(3)(L). An agreement entered into in settlement of the pending dissolution, however, is subject to court approval. Wis. Stat. § 767.34; *Van Boxtel v. Van Boxtel*, 2001 WI 40, 242 Wis. 2d 474, 625 N.W.2d 284. In *Evenson v. Evenson*, 228 Wis. 2d 676, 598 N.W.2d 232 (Ct. App. 1999), after the divorce petition was filed, the parties entered into a "Limited Marital Property Agreement" that dealt, among other things, with the disposition of the wife's stock. The husband sought to repudiate the agreement, but the circuit court enforced it. The court of appeals remanded the matter, holding that the agreement was a divorce settlement agreement subject to court approval under section 767.10(1) (now section 767.34), not a written agreement enforceable under section 767.255(3)(L) (now section 767.61(3)(L)). Similarly, the court in *Ayres v. Ayres*, 230 Wis. 2d 431, 602 N.W.2d 132 (Ct. App. 1999), allowed repudiation of an agreement entered into in connection with a pending divorce. *But see Hottenroth v. Hetsko*, 2006 WI App 249, 298 Wis. 2d 200, 727 N.W.2d 38 (not allowing repudiation of stipulation); *see also Wilke v. Wilke*, 212 Wis. 2d 271, 569 N.W.2d 296 (Ct. App. 1997) (holding that release in settlement agreement, of each party's interest in assets awarded to the other party, acted as release of husband's right to redeem wife's stock in closely held family corporation).

Specific standards apply at dissolution to the enforceability of provisions relating to property division, spousal support, and child support. These specific standards differ from the general standards and are discussed *infra* in the relevant sections.

## B. Property Division [§ 11.38]

If there is a marital property agreement with property-division provisions, section 767.61(3)(L) states that at dissolution such an agreement will be enforced unless “the terms of the agreement are inequitable as to either party.” There is a presumption that the terms are equitable, and the spouse seeking to have it set aside must prove that the agreement is inequitable. Wis. Stat. § 767.61(3)(L). This provision applies to agreements executed before and after the spouses’ determination date. To be enforceable in a dissolution and considered equitable under section 767.61(3)(L), an agreement with property-division provisions must meet the tests of voluntariness and disclosure and must be fair when made, and, if circumstances have substantially changed since the time of execution, at the time of dissolution. *Button v. Button*, 131 Wis. 2d 84, 89, 388 N.W.2d 546 (1986); *see also supra* § 7.140 (discussion of *Button* and tension between tests for enforceability under sections 766.58(6) and 767.255(3)(L) (now section 767.61(3)(L))).

The court of appeals applied the *Button* test in *Warren v. Warren*, 147 Wis. 2d 704, 433 N.W.2d 295 (Ct. App. 1988). The wife’s deferred employment benefits were significantly reduced because of her early retirement. When the parties were divorced, the wife argued that this reduced income was a change in circumstances and that she should not be bound by the parties’ premarital agreement. The court found that her early retirement could have been reasonably contemplated and had in fact been contemplated when the agreement was made. Consequently, the court held that the agreement was equitable at divorce and enforced the agreement. *See supra* § 7.141. The court also stated that once an agreement is found to be equitable, it controls the outcome of the property division under section 767.255(11) (now section 767.61(3)(L)); in other words, the agreement is not merely one of the 13 factors altering the presumptively equal division. *Warren*, 147 Wis. 2d at 711–12. The court withdrew contrary dicta in *Torgerson v. Torgerson*, 128 Wis. 2d 465, 469 n.2, 383 N.W.2d 506 (Ct. App. 1986). *But see Krejci v. Krejci*, 2003 WI App 160, 266 Wis. 2d 284, 667 N.W.2d 780 (holding inequitable enforcement of prenuptial agreement at divorce when wife’s efforts had contributed to appreciation of husband’s inherited property); *Gardner v. Gardner*, 175 Wis. 2d 420, 432, 499 N.W.2d 266 (Ct. App. 1993) (holding that validity of parties’ marital property agreement would not prevent court from providing relief to one spouse under section 767.255(11) (now section 767.61(3)(L)), if it would be equitable to deviate from agreement’s terms); *Pearce v. Pearce*, 824 S.W.2d 195

(Tex. App. 1991) (holding that although wife was precluded by marital agreement from acquiring interest in community property, she was not precluded from claiming reimbursement for husband's use of "community efforts" to improve his separate property); *see also Steinmann v. Steinmann*, 2008 WI 43, ¶ 43, 309 Wis. 2d 29, 749 N.W.2d 145 (holding that income from excluded asset was divisible); *Antuk v. Antuk*, 130 Wis. 2d 340, 387 N.W.2d 80 (Ct. App. 1986) (holding that prenuptial agreement provision covering property "acquired by either prospective spouse before or after marriage" included appreciation of excluded asset, some of which resulted from nonowning spouse's efforts, and excluding such appreciation from marital estate).

Similarly, in *Greenwald v. Greenwald*, 154 Wis. 2d 767, 454 N.W.2d 34 (Ct. App. 1990), the court found that the disclosure requirement was met by one party's actual knowledge of the other party's financial condition and held that the agreement was fair even though its effect was one-sided. The parties were married late in life, and the husband repeatedly insisted that he would marry only on the condition that his assets be preserved for his children from a former marriage. The wife was his former housekeeper, and the court found that she voluntarily accepted the husband's terms. Since the parties' circumstances at the time of the divorce were reasonably anticipated at the time the agreement was executed, the agreement was enforceable under section 767.255(11) (now section 767.61(3)(L)). *See also Gardner v. Gardner*, 190 Wis. 2d 217, 527 N.W.2d 70 (Ct. App. 1994).

For a marital property agreement to be enforceable in a dissolution proceeding, it must contain provisions relating specifically to the dissolution of the marriage. An agreement relating only to disposition at death will not control property division at dissolution. *Levy v. Levy*, 130 Wis. 2d 523, 388 N.W.2d 170 (1986); *see also Webb v. Webb*, 148 Wis. 2d 455, 461–62, 434 N.W.2d 856 (Ct. App. 1988) (holding that although agreement had no specific provision relating to divorce, agreement nevertheless controlled property division, in part because attorney who drafted agreement testified that general waiver of rights was intended to apply to divorce).

Unless a judgment of dissolution provides otherwise, any provisions of a marital property agreement that would pass property at the death of a spouse, a so-called Washington will, are revoked at the time of judgment. Wis. Stat. § 767.375(1); *see Barbara S. Hughes, New Probate Code Affects Estate Planning at Divorce*, Wis. Law., Mar. 1999, at 14.

### **C. Right of Spouse to Support During Marriage and After Dissolution [§ 11.39]**

The modification or elimination of support of a spouse during a marriage is a permissible subject for a marital property agreement. Wis. Stat. § 766.58(3)(d). The agreement may not, however, result in a spouse having less than adequate support during the marriage, taking into consideration all sources available for support. Wis. Stat. § 766.58(9)(a). This is consistent with section 948.22, which makes it a punishable offense for a person to intentionally fail to provide adequate support for a spouse or other dependents without just cause. *See supra* § 11.31.

More specifically, section 766.58(9)(b) sets an objective standard for determining whether provisions of marital property agreements relating to spousal support after dissolution are enforceable:

If a marital property agreement modifies or eliminates spousal support so as to make one spouse eligible for public assistance at the time of dissolution of the marriage or termination of the marriage by death, the court may require the other spouse or the other spouse's estate to provide support necessary to avoid that eligibility, notwithstanding the marital property agreement.

Even if a marital property agreement limiting or eliminating support at the time of dissolution does not leave a spouse with less than adequate support or eligible for public assistance, the court is not bound by such a provision. Section 767.56(8) requires that a court only “consider” an agreement in setting maintenance. This section was unchanged by the Act. In a dissolution action the court could use its discretion to refuse to follow a provision reducing or eliminating support.

A court need not enforce an agreement limiting maintenance at the time of dissolution, but an agreement for nonmodifiable maintenance after dissolution is not against public policy. *Nichols v. Nichols*, 162 Wis. 2d 96, 100, 469 N.W.2d 619 (1991) (citing *Rintelman v. Rintelman*, 118 Wis. 2d 587, 348 N.W.2d 498 (1984)). The party seeking a modification of maintenance can be estopped by the agreement from receiving a modification. *Id.* Four conditions must be met for estoppel to apply: (1) the agreement must be incorporated into the judgment of dissolution; (2) the agreement must be part of a comprehensive property settlement approved by the court; (3) the agreement must be fair, equitable, not illegal, and not against public policy; and (4) the party seeking to be released from the agreement must be doing so on the

ground that the court did not have the power to enter the order without the party's agreement. *Id.* But see *Patrickus v. Patrickus*, 2000 WI App 255, 239 Wis. 2d 340, 620 N.W.2d 205 (refusing to apply equitable estoppel to marital settlement agreement that was unfair because it allowed wife to seek increase in maintenance but did not allow husband to seek decrease as a result of decreased income). Although the agreements enforced in *Nichols* and *Rintelman* were entered into at the time of the dissolution, the same reasoning might apply to a marital property agreement enforced at the time of dissolution. See also Patricia K. Ballman, *Drafting Divorce Provisions in Marital Agreements*, 8 Wis. Law. Marital Prop. F. 1 (1991).

The question of enforceability arises if support is provided under a marital property agreement for a period of time after the decree and is then eliminated, thus causing the payee to become eligible for public assistance. A similar result might occur if a spouse receives a series of payments as a property division, with no maintenance, and he or she becomes eligible for public assistance after the payments cease. Such eligibility would occur after, not at the time of, the dissolution. The issue is whether including a provision for a short period of maintenance will avoid the application of section 766.58(9)(b). A spouse requesting an extension of maintenance before it is eliminated may be granted such an extension. See *Dixon v. Dixon*, 107 Wis. 2d 492, 508, 319 N.W.2d 846 (1982). Absent such a timely request by the payee spouse, however, it appears that the payor spouse could not be compelled to provide further support.

A marriage agreement entered into before the Act that eliminated spousal support after dissolution would not be limited by section 766.58(9)(a) or (b). However, section 767.56(8) requires that a court only “consider” a marriage agreement as it relates to spousal support. See *supra* § 7.140. If a spouse becomes eligible for public support at the time of divorce, it is highly unlikely that a court would follow the agreement. See *supra* § 4.92 (regarding spouse's eligibility for medical assistance (Medicaid)).

## **D. Child Support [§ 11.40]**

A marital property agreement may not adversely affect the right of a child to support. Wis. Stat. § 766.58(2). Therefore, provisions limiting or eliminating a spouse's obligation to support a child or limiting the



authority of a court to modify support upon a change of circumstances will not be enforced. *Motte v. Motte*, 2007 WI App 111, 300 Wis. 2d 621, 731 N.W.2d 294; *Wood v. Propeck*, 2007 WI App 24, 299 Wis. 2d 470, 728 N.W.2d 757; *Ondrasek v. Tenneson*, 158 Wis. 2d 690, 462 N.W.2d 915 (Ct. App. 1990). On the other hand, the court may enforce provisions enhancing a child's support, such as provisions to fund a college education or to support adult children or children not born to or adopted by the payor, whom the spouse would not otherwise be obligated to support. *See Bliwas v. Bliwas*, 47 Wis. 2d 635, 178 N.W.2d 35 (1970); *Honore v. Honore*, 149 Wis. 2d 512, 439 N.W.2d 827 (Ct. App. 1989). A provision that places a limit on child support notwithstanding the payor's income is against public policy. *Ondrasek*, 158 Wis. 2d 690; *see also supra* § 11.34. An agreement that prohibits consideration of a change in circumstances, even if it decreases child support, is likewise unenforceable. *Krieman v. Goldberg*, 214 Wis. 2d 163, 571 N.W.2d 425 (Ct. App. 1997). Nevertheless, if the child's needs are being met, a child support agreement may be enforced even if it differs from the percentage standards. *Zutz v. Zutz*, 208 Wis. 2d 338, 559 N.W.2d 919 (Ct. App. 1997) (refusing to modify prior agreement because child's needs were being met, notwithstanding change in both parties' circumstances).

### **E. Statutory Agreements [§ 11.41]**

Chapter 766 includes two statutory marital property agreements. Wis. Stat. §§ 766.588, .589. These agreements are discussed in sections 7.73–.92, *supra*, and are reproduced in sections 7.173–.177, *supra*. By specific statutory provision, neither of these agreements may apply to or affect property division or support obligations at the dissolution of a marriage. Wis. Stat. §§ 766.588(6), .589(6).

## **V. Nonmarital Relationships and Invalid Marriages [§ 11.42]**

### **A. Nonmarital Relationships [§ 11.43]**

Chapter 766 does not apply when there is no determination date. *See* Wis. Stat. § 766.03(1). If both parties to a relationship know they are not married, the policies of the Act do not become applicable, because the Act applies only to spouses. *See* Wis. Stat. § 765.001(2). It does not

apply to so-called common law marriages, which are not recognized in Wisconsin, although a common law marriage that is valid in another state in which the spouses resided when the common law marriage became effective would be given legal effect in Wisconsin. Wis. Stat. §§ 765.16, .21.

A long-standing relationship may, nevertheless, have many of the characteristics of a marriage without the ceremony, and the law has moved toward recognizing obligations that may result. The Wisconsin Supreme Court has held that even though section 767.255 (now section 767.61) does not apply, in the proper circumstances unmarried cohabitants may raise claims against each other, at the termination of their relationship, based on express or implied contract, quasi-contract, partnership, constructive trust, or resulting trust. A cohabiting nonmarital partner attempting to recover from the other partner must show a shared enterprise and proof that contributions by the plaintiff resulted in an increase in assets. *Watts v. Watts*, 137 Wis. 2d 506, 405 N.W.2d 303 (1987), *later proceeding*, 152 Wis. 2d 370, 448 N.W.2d 292 (Ct. App. 1989); *Lawlis v. Thompson*, 137 Wis. 2d 490, 405 N.W.2d 317 (1987); *Ulrich v. Zemke*, 2002 WI App 246, 258 Wis. 2d 180, 654 N.W.2d 458 (holding that court must look at entire shared enterprise and should not analyze claim asset by asset); *Meyer v. Meyer*, 2000 WI App 12, 232 Wis. 2d 191, 606 N.W.2d 184 (holding that it was unfair to use fixed salary to value medical degree and that degree is not an asset for unjust-enrichment determination); *Ward v. Jahnke*, 220 Wis. 2d 539, 583 N.W.2d 656 (Ct. App. 1998) (remanding for determination of damages because increase in assets after purchase of house not proved); *Waage v. Borer*, 188 Wis. 2d 324, 525 N.W.2d 96 (Ct. App. 1994) (holding that increase in assets was not proved). Fraud or estoppel may also support recovery by one party in a nonmarital relationship. *See also Connell v. Francisco*, 898 P.2d 831 (Wash. 1995) (under Washington law, court divided property that would have been community property if parties were married); *Chesterfield v. Nash*, 978 P.2d 551 (Wash. Ct. App. 1999) (under Washington law, holding that there is rebuttable presumption that property acquired by both parties during relationship is owned by both parties); *Foster v. Thilges*, 812 P.2d 523 (Wash. Ct. App. 1991) (under Washington law, holding that property of parties cohabiting in long-term “pseudomarital relationship” may be equitably divided); *Has the Door Been Opened for the Recognition of Palimony in Wisconsin?*, 22 Wis. J. Fam. L. 8 (2002); Marianne M. Jennings & Bruce K. Childers, *Property Rights of Unmarried Couples: Who Gets What When the Cohabitation Collapses?*, 6 Community Prop. J. 258 (1979);

Linda J. Ravdin, *The Next Wave of Domestic Partner Litigation: Why Domestic Partners Need Partnership Agreements*, 14 Divorce Litig. 137 (Aug. 2002); N. Roddy, *Rights and Remedies of Cohabiting Couples upon Termination of the Relationship*, 4 Divorce Litig. 209 (1992); Alvin R. Wohl & Helene A. Winnick, *Palimony—A Trial Run*, 9 Community Prop. J. 15 (1982). However, such remedies must be found outside the Act. Chapter 766, titled “Property Rights of Married Persons; Marital Property,” applies only to spouses.

## **B. Invalid Marriages; Putative Spouses [§ 11.44]**

Under some circumstances, through mistake or deceit, one or both parties to a relationship may believe there is a valid marriage when in fact there is not. This is most likely to occur when one spouse fails to obtain a valid divorce and participates in a subsequent marriage ceremony with another person. The law should treat the innocent party or parties equitably with respect to property interests that arise during the putative marriage. Section 766.73, titled “Invalid Marriages,” provides:

If a marriage is invalidated by a decree, a court may apply so much of this chapter to the property of the parties to the invalid marriage as is necessary to avoid an inequitable result. This section does not apply if s. 767.61 applies to the action to invalidate the marriage.

It is important to note that a decree declaring the marriage invalid is necessary for this section to apply. A marriage is presumed valid until a court declares it otherwise. Section 767.61(1) requires that a property division be made in every “judgment of annulment, divorce or legal separation.” See also Wis. Stat. § 767.313 (circumstances under which court may annul marriage). Therefore, it is not clear when, if ever, section 766.73 would be applied. If the marriage is found to be invalid without a decree, such as for the purpose of determining inheritance tax, this section authorizing equitable allocation will not apply, and title will determine ownership. See *Estate of Steffke v. Wisconsin Dep’t of Revenue (In re Estate of Steffke)*, 65 Wis. 2d 199, 222 N.W.2d 628 (1974).

Under historical community property principles, a putative marriage is one in which at least one spouse was unaware of any impediment to the marriage and believed the marriage to be valid. According to William Q. de Funiak & Michael J. Vaughn, *Principles of Community*

*Property* §§ 56, 222 (2d ed. 1971), the rules of community property apply to such a marriage; however, if there is a legal spouse, perhaps because of an invalid divorce, and if other equitable doctrines such as estoppel do not apply, then the legal spouse does not lose his or her interest in community property assets acquired by the spouse who has entered into another relationship. *Id.* The legal spouse owns one-half of the community property, the putative spouse owns the other half, and the spouse who wrongfully entered into the putative marriage receives nothing. The innocent party in a putative marriage may claim a community interest, while the spouse who did not act in good faith can make no claim to the property. *Id.* If bad faith exists with both parties, there is no community. *Id.* Conceivably, there could be three innocent parties, in which case a court's general equity powers would probably come into play. *See also supra* § 6.46 (rights of creditors after marriage is annulled).

California law provides that a good-faith party in a putative marriage is to receive as much of the marital estate as he or she would have received under community property concepts. Cal. Fam. Code Ann. § 2251 (West, WESTLAW current with all 2009 Reg. Sess. laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. laws; urgency legislation through Ch. 14 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot). The court may also take into consideration the actions of the good- and bad-faith parties, however, and review the contributions to the estate. *Redmond v. Redmond*, 10 Fam. L. Rep. (BNA) 1559 (Cal. Ct. App. 1984) (unpublished opinion). Since an equitable division is provided for in Wisconsin when a marriage is found to be invalid, cases arising under the California statute may be helpful in determining property division under sections 766.73 and 767.61. *See also Osuna v. Quintana*, 993 S.W.2d 201 (Tex. App. 1999) (putative marriage terminated when wife learned of husband's prior undissolved marriage).

Section 767.61(1) indicates that the court is to use the same equitable considerations in dividing property in an annulment as are used for a divorce or legal separation. *See Siskoy v. Siskoy*, 250 Wis. 435, 27 N.W.2d 488 (1947). Since both sections 766.73 and 767.61 provide for equitable division of property in an annulment, the result should be the same if section 766.61 is applied instead of section 766.73.

## Estate Administration and Nonprobate Transfers

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## I. Introduction: UMPA Is a Property Law [§ 12.1]

The Uniform Marital Property Act (UMPA, reprinted *infra* app. A) is a property statute that determines ownership of property. It does not contain provisions governing the distribution of property after the termination of the marriage by dissolution or death. The prefatory note to UMPA states in part as follows:

FOURTH: On dissolution the structure of the Act as a *property statute* comes into full play. The Act takes the parties “to the door of the divorce court” only. It leaves to existing dissolution procedures in the several states the selection of the appropriate procedures for dividing property. On the other hand, the Act has the function of confirming the *ownership* of property as the couple enters the process. Thus reallocation of property derived from the effort of both spouses during the marriage starts from a basis of the equal undivided ownership that the spouses share in their marital property. A given state’s equitable distribution or other property division procedures could mean that the ownership will end that way, or that it could be substantially altered, but that will depend on other applicable state law and judicial determinations. *An analogous situation obtains at death, with the Act operating primarily as a property statute rather than a probate statute.*

(Emphasis added to final sentence.) As the prefatory note indicates, states that adopt UMPA must fit the uniform act into their existing dissolution and probate law procedures. The Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or the

Wisconsin Marital Property Act], therefore includes provisions not found in UMPA concerning estate administration and nonprobate transfers.<sup>1</sup>

## **II. Estate Administration of Marital Property Assets: Administering Decedent's Interest vs. Both Spouses' Interests [§ 12.2]**

The comment to UMPA section 18 states in part as follows:

*The Administration Issue:* Historically the entire community was administered when a spouse died. See William Q. de Funiak and Michael J. Vaughn, *Principles of Community Property*, §§ 205–07 (1971). This pattern has been eroding. At this time [1983], California and Nevada require administration only of the decedent's interest in the community. Arizona, Idaho, New Mexico and Washington follow the traditional pattern, though all four have simplified administration procedures under their versions of the *Uniform Probate Code* or Washington's non-intervention provision. Texas and Louisiana have simplified procedures when there is a surviving spouse but no issue, in Texas, or when succession without administration occurs, in Louisiana. In addition, Texas has independent administration as a possibility. An adopting state will necessarily face the administration issue and will be forced to consider whether the California and Nevada solution represents the appropriate trend.

(Citation omitted.)

Wisconsin adopted the California and Nevada solution. Section 861.01(2) provides that when a spouse dies, the surviving spouse retains his or her undivided one-half interest in each marital property asset. The surviving spouse's interest is a tenancy in common, and the decedent's successor (for example, the personal representative) is a tenant in common with the surviving spouse. Wis. Stat. § 861.01(1). The

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as affected by acts through 2009 Wisconsin Act 189; all references to the Internal Revenue Code (I.R.C.) are current through Public Law No. 111-156 (excluding Pub. L. Nos. 111-148 and 111-152) (Apr. 7, 2010); and all references to the Code of Federal Regulations are current through 75 Fed. Reg. 18,375 (Apr. 9, 2010). Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

surviving spouse's marital property interest is not subject to administration. *Id.*

For some probate procedures (as distinguished from substantive law), the system under the Wisconsin Marital Property Act does not differ significantly from the former common law system. When one spouse dies, marital property assets subject to administration become tenancy-in-common property. Wis. Stat. § 861.01(2). The probate forms and procedures that existed before passage of the Act were adequate for the administration of tenancy-in-common property. However, the two systems differ significantly with respect to other probate procedures and practice:

1. The decedent's interest in former marital property assets must be determined. All the classification and mixing rules described in chapters 2 and 3, *supra*, must be applied. Fractional ownership interests in assets occur much more frequently under the Act than under the former common-law property system. The decedent may have a marital property interest in assets previously thought to be the surviving spouse's. Assertion of this interest by the decedent's personal representative is a procedure that was new with the Act.
2. The management and control rules of chapter 766 apply during probate. Wis. Stat. §§ 861.01(1), 857.01, .015.
3. The Act's rules regarding satisfaction of obligations considerably affect the procedure for claims.
4. The deferred marital property election under the Act replaced the surviving spouse's one-third elective share under the former common-law property system. *See* Wis. Stat. § 861.02.

### III. Nonprobate Transfers [§ 12.3]

#### A. Distinction Between Probate and Nonprobate Transfers [§ 12.4]

##### 1. In General [§ 12.5]

In Wisconsin, a decedent's interest in property is transferable at death either by intestate or testamentary (*probate*) means or by nontestamentary (*nonprobate*) means. Usually, when a spouse dies, both means are used to transfer property interests. The Wisconsin Marital Property Act did not change this historical scheme for transferring property at death. Therefore, when a spouse dies, his or her property may be transferred to designated beneficiaries by nonprobate means or may be subject to probate administration, by the personal representative, with or without the supervision of the probate court.

Nonprobate means of transfer are also referred to as *will substitutes*. The many types of will substitutes permit a decedent to own or enjoy property during his or her lifetime and to transfer it other than by will at death. The following are some of the more common will substitutes:

1. Joint tenancies with right of survivorship;
2. Joint accounts held at financial institutions, stock brokers, and mutual-fund companies;
3. Survivorship marital property;
4. Marital property agreements containing dispositive provisions;
5. Revocable living trusts containing dispositive provisions;
6. Life insurance, annuities, and other products issued by life insurance companies payable to someone other than the decedent's estate or having transfer of ownership provision at death;

➤ **Note.** In *Jung v. Jung*, 2000 WI App 151, 237 Wis. 2d 853, 616 N.W.2d 118, the decedent spouse owned an annuity as individual property. The annuity contract had a provision providing for a transfer of ownership at his death to his spouse.

The court of appeals held that the transfer of ownership provision in the annuity contract governed the disposition of the decedent's ownership interest at death.

7. Deferred employment benefits payable to someone other than the decedent's estate;
8. Payable on death (P.O.D.) accounts and P.O.D. bonds payable to someone other than the decedent's estate; and
9. Transfer on death (T.O.D.) provisions pursuant to sections 705.10 and 705.15.

## **2. Gifts of Marital Property Assets During Lifetime Contrasted with Gifts of Interest in Marital Property Assets at Death [§ 12.6]**

### **a. In General [§ 12.7]**

The Act contains provisions dealing with (1) one spouse's gifts of marital property assets during that spouse's lifetime, and (2) one spouse's gifts of an interest in marital property at that spouse's death. These provisions are discussed in sections 12.8–.10, *infra*.

### **b. Gifts of Marital Property Assets During Lifetime [§ 12.8]**

Under the Act, one spouse who has the right, acting alone, to manage and control marital property assets may make gifts of marital property assets to third persons. Wis. Stat. § 766.51(4); Wis. Stat. Ann. § 766.51(4) Legis. Council Comm. Supplemental Notes Relating to 1985 Act 37 (West 2009). 1985 Wisconsin Act 37 is referred to as the 1985 Trailer Bill. Section 766.53 provides that a spouse acting alone may give marital property to a third person *only* if the aggregate value of the marital property assets when given to the third person does not exceed \$1,000 in a calendar year or a larger amount, if reasonable. The 1985 Trailer Bill amended section 766.51(4) to clarify that the power of management and control applies to gifts that exceed the safe-harbor



amounts in section 766.53. Section 766.53 should be amended to conform to section 766.51(4). However, if gifts by one spouse to a third person of marital property assets during the marriage exceed the safe-harbor limits in section 766.53, the other spouse (or that spouse's estate) has a remedy against the donating spouse (or the donating spouse's estate), the donee, or both. Wis. Stat. § 766.70(6)(a); *see supra* §§ 4.37, 8.45; *see also infra* § 12.12. Under section 766.70(6)(a), the nondonating spouse may bring an action to recover the property or a compensatory judgment.

➤ **Note.** The remedies provided by the Wisconsin Marital Property Act, in particular those provided by section 766.70, are the exclusive remedies for a spouse who disputes a transfer of marital property. *Jackson v. Employe Trust Funds Bd.*, 230 Wis. 2d 677, 602 N.W.2d 543 (Ct. App. 1999); *Socha v. Socha*, 204 Wis. 2d 474, 481, 555 N.W.2d 152 (Ct. App. 1996); *see also Joyce v. Joyce (In re Estate of Joyce)*, 2008 WI App 92, 312 Wis. 2d 745, 754 N.W.2d 515.

### **c. Gifts of Marital Property Assets at Death of One Spouse [§ 12.9]**

If one spouse dies having made a nonprobate disposition of marital property assets to a third person, the surviving nondonor spouse has a remedy against the third person under section 766.70(6)(b). However, the remedy differs from the remedy available for gifts made by one spouse during the marriage. Under section 766.70(6)(a), which applies to gifts during marriage, the nondonating spouse may recover the property donated or a compensatory judgment as marital property. Under section 766.70(6)(b), which applies to nonprobate transfers at death, the surviving spouse may recover one-half of the gift of marital property from the recipient as his or her own property; the surviving spouse has no remedy against the decedent's estate. Since the surviving spouse's remedy is limited to one-half of the marital property given, the first spouse to die may effectively give his or her one-half interest in marital property to a third person by nonprobate means. Such a gift of a one-half interest that severs the spouse's interests is not possible during the marriage.

➤ **Note.** The remedies provided by the Marital Property Act, in particular those provided by section 766.70, are the exclusive

remedies for a spouse who disputes a nonprobate transfer of marital property. *Jackson*, 230 Wis. 2d 677; *Socha*, 204 Wis. 2d at 481; *see also Joyce*, 2008 WI App 92, 312 Wis. 2d 745.

A spouse's nonprobate transfers are arranged while that spouse is alive. If that spouse has the right, acting alone, to manage and control a certain asset, that spouse may transfer the entire asset at death by nonprobate means, subject to the surviving spouse's remedy. For example:

1. The record owner of a life insurance policy may designate a third person as the sole beneficiary of the proceeds. *See* Wis. Stat. § 766.51(1)(d). Section 766.61(2) permits life insurance companies to make payments in accordance with the policy. If the proceeds are marital property and the insurance company pays all the proceeds to the third person, the third person receives the surviving spouse's interest in the proceeds subject to the surviving spouse's remedy under section 766.70(6)(b).
2. Subject to possible application of other laws, an employee spouse may designate a third person as the sole beneficiary of deferred employment benefits. *See* Wis. Stat. § 766.51(1)(e). Section 766.62(4) permits a deferred-employment-benefit plan administrator to make payments in accordance with the plan. Receipt by the third person is subject to the surviving spouse's remedy under section 766.70(6)(b).
  - **Note.** Federal law restricts a spouse's right to designate a third person as beneficiary of certain deferred-employment-benefit plans. *See supra* ch. 2. Wisconsin law restricts the choice of retirement annuities by a participant under the Wisconsin Retirement System. Wis. Stat. § 40.24(7).
3. If marital property is used to create a joint tenancy with right of survivorship with a third person, the incidents of the joint tenancy control, *see* Wis. Stat. § 766.60(4)(a), subject to the nondonating spouse's remedy against the surviving tenant or the decedent's estate under section 766.70(6)(c).
4. Financial institutions may make payments in accordance with multiple-party-account contracts, *see* Wis. Stat. 705.06, subject to the

surviving spouse's remedy against the recipient under section 766.70(6)(b).

5. Marital property in a revocable trust containing dispositive provisions is managed by the trustee according to the terms of the trust document, Wis. Stat. § 766.51(3), subject to the surviving spouse's remedy under section 766.70(6)(b).
6. If marital property is used to purchase a United States bond and the bond is registered in joint names or made payable on death to a third person, federal regulations control the disposition of the bond when one spouse dies, 31 C.F.R. §§ 353.70–71, subject to the surviving spouse's remedy under section 766.70(6)(b). See section 12.14, *infra*, with respect to federal preemption.

#### **d. Effect of Nonprobate Disposition on Surviving Spouse's Marital Property Interest [§ 12.10]**

Subsection 861.01(1) provides that when one spouse dies, the surviving spouse retains his or her undivided one-half ownership interest in each item of marital property. Subsection 861.01(2) provides that when a third party succeeds to the decedent's interest in marital property, that third party is a tenant in common with the surviving spouse. Subsections 861.01(1) and (2) appear to be limited to property that is subject to administration.

If a spouse having the right of management and control makes a gift of a marital property asset to a third person during the marriage, the gift is complete at the time it is made. Wis. Stat. Ann. § 766.51(4) Legis. Council Comm. Supplemental Notes Relating to 1985 Act 37 (West 2009). The nondonating spouse has the choice of bringing an action to recover the property given or to receive a compensatory judgment equal to the amount by which the gift exceeded the safe-harbor limits in section 766.53. Wis. Stat. § 766.70(6)(a).

When a spouse with management and control rights arranges for a nonprobate disposition of marital property assets, does the surviving spouse retain his or her ownership interest, as happens when there is a probate disposition of marital property assets, or is the surviving spouse

divested of ownership, as happens when there is a lifetime gift? Section 766.70(6)(b) permits the surviving spouse to bring an action with respect to certain types of transfers against the gift recipient to recover “one-half of the gift of marital property.” The meaning of section 766.70(6)(b) is not clear from a reading of the statute. To harmonize the various sections involved (sections 766.53, 766.70(6)(a) and (b), and 861.01(1) and (2)), the logical conclusion is that a nonprobate disposition of marital property assets is analogous to a lifetime gift of marital property assets, with the result that the surviving spouse is divested of an ownership interest and has a remedy to recover an amount from the beneficiary of the nonprobate disposition rather than half the property itself. However, section 766.70(6)(b) can be interpreted to mean that the surviving spouse can recover half of the particular item of nonprobate property given away.

In summary, if a spouse having the right of management and control makes either a lifetime gift effective during marriage or a nonprobate disposition of marital property assets effective at death, the nondonating spouse is divested of any ownership interest in the donated property but has remedies. Subsection 766.70(6)(a) provides the remedy for lifetime gifts. Subsections 766.70(6)(b) and (c) provide the remedies for nonprobate dispositions. If a spouse dies owning marital property assets subject to administration, the surviving spouse retains his or her marital property interest whether or not the decedent spouse attempted to make a testamentary disposition of the survivor’s marital property interest. Sometimes, however, the decedent’s attempt to dispose of the surviving spouse’s interest in a marital property asset may put the surviving spouse to an equitable election. *See infra* §§ 12.22–.26.

Generally, there are no restrictions on a spouse’s lifetime gifts of nonmarital property assets. The nondonating spouse has no remedy during the marriage for a gift of nonmarital property assets. However, if a nonmarital property asset is given away by the owner spouse during the marriage and the asset given away is deferred marital property, the provisions of the deferred marital property election may apply if the gift was made within two years of death or the donor retained certain rights. Wis. Stat. § 861.02; *see infra* § 12.11. Thus, lifetime gifts of deferred marital property assets are subject to a two-year rule, whereas lifetime gifts of marital property assets are not. In addition, the surviving spouse has certain remedies for fraudulent transfers; these remedies apply regardless of the property’s classification. Wis. Stat. § 861.17; *see infra* § 12.168.

### 3. Gifts of Deferred Marital Property Assets During Lifetime [§ 12.11]

The augmented deferred marital property estate includes the value of any deferred marital property transferred by the decedent within the two years immediately preceding the decedent's death. Wis. Stat. § 861.03(4)(b); *see infra* § 12.155. Original recipients of the decedent's transfers of deferred marital property are personally liable to make a prorated contribution toward satisfaction of the surviving spouse's deferred marital property elected amount. Wis. Stat. § 861.07(2). The recipient has the option of returning a portion or all of the gift or paying a monetary amount. Wis. Stat. § 861.07(3).

Section 861.10(1) provides that a waiver of the right to make the deferred marital property election must be contained in a marital property agreement that is enforceable under section 766.58 or in a signed document filed with the probate court. *See infra* § 12.140 (waiver of right to elect). Thus, it would appear that a simple joinder or consent to a gift of deferred marital property is insufficient to waive the elective right. However, section 861.05(1)(c) provides that gifts of deferred marital property with the written joinder or written consent of the nondonee spouse are excluded from the augmented deferred marital property estate.

➤ **Note.** The section 861.05(1)(c) standard of “written joinder or written consent” for purposes of the deferred marital election differs from the section 766.53 standard of “act together” for purposes of lifetime gifts. Section 861.05(1)(c) requires a writing. “Acting together” in section 766.53 does not require a writing. The filing of a tax return reflecting the gift signed by both spouses satisfies the tests of sections 861.05(1)(c) and 766.53. *See supra* ch. 4, ch. 9.

### B. Remedies of Surviving Spouse [§ 12.12]

If the predeceasing spouse makes a nonprobate disposition, to a third person, of an asset that is marital property or that has a marital property component, the Act provides remedies by which the surviving spouse may recover his or her former marital property interest in the asset. *See* Wis. Stat. § 766.70(6)(b), (c).

If a transfer of a marital property asset to a third person during marriage by a spouse acting alone becomes a completed gift upon the spouse's death, or if an arrangement during marriage made by one spouse acting alone involving marital property is intended to be and becomes a gift to a third person upon the spouse's death, the surviving spouse may bring an action against the gift recipient to recover one-half of the gift of marital property. Wis. Stat. § 766.70(6)(b)1. This provision is intended to apply, *inter alia*, to multiple-party accounts under chapter 705, revocable trusts, life insurance policies, and certain bonds. Wis. Stat. Ann. § 766.70(6)(b) Legis. Council Notes—1985 Act 37, §§ 89, 130 to 138 (West 2009).

➤ **Comment.** It is not clear whether “one-half of the gift of marital property” requires that the actual item transferred be divided in half or whether the surviving spouse has a claim for an amount. The better view is that the spouse has a claim.

If marital property is used by one spouse acting alone to create a joint tenancy with right of survivorship with a third person, the incidents of the joint tenancy control. Wis. Stat. § 766.60(4)(a). However, if the spouse has given a gift of a marital property asset in the form of a joint tenancy, the nondonating spouse has a remedy under section 766.70(6)(c). *See supra* § 8.48.

➤ **Note.** The remedies provided by the Marital Property Act, in particular those provided by section 766.70, are the exclusive remedies for a spouse who disputes a transfer of marital property. *Jackson*, 230 Wis. 2d 677; *Socha*, 204 Wis. 2d at 481.

See chapter 8, *supra*, for further discussion of remedies.

### C. Statutes of Limitation [§ 12.13]

If one spouse effects a donative nonprobate disposition of marital property assets to a third person, the surviving spouse must commence an action within a time limit under the remedy statutes. Section 766.70(6)(b)1. states that the surviving spouse may not commence an action under section 766.70(6)(b) later than one year after the death of the decedent spouse. *Jackson*, 230 Wis. 2d 677; *see also Joyce*, 2008 WI App 92, 312 Wis. 2d 745. Section 766.70(6)(b)1. applies if the spouse effecting the nonprobate disposition predeceases the nondonating spouse.

If the nondonating surviving spouse dies before commencing the action, that spouse's personal representative may commence the action within the original time limits.

The nondonating spouse might predecease the spouse who arranged for the nonprobate disposition. Usually, if the nondonating spouse predeceases the donor spouse, the nondonating spouse's marital property interest in the asset is subject to administration. The surviving spouse is a tenant in common with the nondonating spouse's personal representative or other successor.

The situation is more complex when both spouses die. Assume that the nondonating spouse dies first and that the donor spouse dies 10 days later. The surviving spouse (the donor) may effect a nonprobate disposition of former marital property assets. In that event, the nondonating spouse's personal representative (or other successor) may commence an action within a limited time to recover the nondonating spouse's former marital property interest. Section 766.70(6)(b)2. provides that if the nondonating spouse predeceases the donor spouse, no action may be commenced later than one year "after the decedent's death." Unfortunately, it is not clear which decedent is referred to in section 766.70(6)(b)2. when both spouses have died. To be consistent with section 766.70(6)(b)1., the one-year period should begin to run from the death of the donor spouse.

Another ambiguity in section 766.70(6)(b)2. is that the recovery is "valued at the date of death of the spouse entitled to recover." This provision makes no sense and appears to be an error in the statute. The nondonating spouse's personal representative should be able to recover one-half the value of the former marital property asset that was given away, valued as of the date of the donor spouse's death.

It appears that the purpose of subdividing section 766.70(6)(b) into subsections 1. and 2. was to subject the recipient of the nonprobate disposition to the same one-year limitation period no matter which spouse dies first.

Subsections 766.70(6)(b)1. and 2. and the questions discussed above may be illustrated by the following examples.

➤ **Example 1.** A husband is the insured and the record owner of a term life insurance policy having a death benefit of \$100,000 and a

fair market value of \$50 (unearned premium). The husband designates his brother as the beneficiary of the policy. The policy is marital property. The husband predeceases his wife.

Under section 766.70(6)(b)1., the wife has one year after her husband's death to commence an action to recover one-half of the \$100,000 proceeds. *Jackson*, 230 Wis. 2d 677; *see also Joyce*, 2008 WI App 92, 312 Wis. 2d 745.

➤ **Example 2.** Same facts as Example 1, except the wife predeceases the husband. The wife has a will leaving everything to her children.

The insurance policy is marital property. The value of the wife's interest in the insurance policy is frozen at its \$25 value on her death. Wis. Stat. § 766.61(7). The husband has the option to purchase his wife's frozen one-half interest in the policy under section 766.70(7). If the husband does not purchase his wife's frozen one-half interest, the husband and the beneficiaries of his wife's estate will be tenants in common of the policy. Questions as to the payment of premiums, right to exercise incidents of ownership during the insured's lifetime, and so forth should be resolved if the surviving spouse does not purchase the decedent's frozen interest.

➤ **Example 3.** Same facts as example 2, except the husband dies 10 days after his wife dies. The proceeds are paid to the husband's children.

In the third example, section 766.70(6)(b)2. applies because marital property assets have in fact been given to a third person. The wife's personal representative (or other successor) has one year from the husband's death to commence an action to recover the wife's frozen marital property interest, which has a value of \$25. The freezing of the wife's interest at \$25 appears to be an unfair result, but section 766.61(7) is clear.

The above examples involve life insurance policies. The same issue will arise in other uses of nonprobate dispositions such as funded revocable living trusts.



➤ **Note.** If the nondonating spouse has a right of recovery with respect to a nonprobate disposition of marital property assets but does not commence an action to recover one-half of the marital property component of the property within the applicable time limit, the remedy is barred. *Jackson*, 230 Wis. 2d 677. A gift subject to federal gift tax laws may result. See *supra* ch. 9; see also *Joyce*, 2008 WI App 92, 312 Wis. 2d 745.

For further discussion of remedies with respect to nonprobate transfers, see sections 8.46–.49, *supra*.

## **D. United States Obligations [§ 12.14]**

Before the Act, section 851.61 provided as follows:

Where a resident of this state dies possessed of bonds or certificates of indebtedness of the United States of America which are registered in his name, payable on death to another, the unqualified ownership and the proceeds shall, on the death of the original owner, belong to the named alternate payee, any law of this state to the contrary notwithstanding.

The Act repealed section 851.61. Presumably, there was concern that one spouse could use section 851.61 to effect a nonprobate disposition of his or her one-half interest in marital property bonds or certificates. For example, one spouse could use marital property to purchase U.S. bonds payable to a third person.

The Code of Federal Regulations, 31 C.F.R. §§ 353.70, .71, permits U.S. bonds to be registered in two ways, either of which results in a nonprobate disposition when the registered owner dies. United States bonds may be registered jointly or registered in the name of one person and payable on death to another.

In *Yiatchos v. Yiatchos*, 376 U.S. 306 (1964), the husband invested Washington community property in U.S. savings bonds. The husband was the registered owner of the bonds, which were payable on his death to his brother. After the husband's death, the brother asserted that he was the sole and absolute owner of the bonds. The U.S. Supreme Court held that federal regulations that have the force of law cannot be used as a shield for fraud or to prevent relief in situations in which the circumstances manifest fraud or a breach of trust tantamount to fraud.

The Supreme Court remanded the case to the Washington Supreme Court for a decision on whether the wife had an ownership interest in the bonds under state law. The U.S. Supreme Court implied that it would not take much to show fraud if indeed the bonds were community property.

➤ **Comment.** A fascinating sidelight of this 1964 case is that the lawyers who argued the case openly stated that they did not know whether Washington's community property regime had an item-by-item rule or an aggregate rule. *See supra* § 10.10. One would think that issue would have been settled by 1964.

In Wisconsin, if the federal regulations for U.S. bonds are used by one spouse to effect a nonprobate disposition of marital property, the disposition occurs in accordance with the regulations. However, it appears there is no preemption with respect to ownership under Wisconsin property law. Therefore, the nondonating spouse seems to have a remedy under section 766.70(6)(b). This is the same remedy that exists for other nonprobate transfers, such as life insurance and multiple-party accounts.

## IV. Intestacy [§ 12.15]

### A. In General [§ 12.16]

Chapter 852 governs the disposition of a decedent's interest in property subject to administration if the decedent does not leave a will that is admitted to probate. It does not apply to property that is not subject to administration.

Subsections 852.01(a) and (b) provide as follows:

**852.01. Basic rules for intestate succession.** (1) Who are heirs. Except as modified by the decedent's will under s. 852.10 (1), any part of the net estate of a decedent that is not disposed of by will passes to the decedent's surviving heirs as follows:

(a) To the spouse or domestic partner:

1. If there are no surviving issue of the decedent, or if the surviving issue are all issue of the surviving spouse or surviving domestic partner and the decedent, the entire estate.

2. If there are surviving issue one or more of whom are not issue of the surviving spouse or surviving domestic partner, one-half of decedent's property other than the following property:

a. The decedent's interest in marital property.

b. The decedent's interest in property held equally and exclusively with the surviving spouse or surviving domestic partner as tenants in common.

(b) To the issue, per stirpes, the share of the estate not passing to the spouse or surviving domestic partner under par. (a), or the entire estate if there is no surviving spouse or surviving domestic partner.

The reason for limiting a tenancy in common to an equal interest is not clear. Tenancy in common interests need not be equal.

## **B. Decedent Leaves Surviving Spouse and No Issue**

### **[§ 12.17]**

If the decedent leaves a surviving spouse and no issue, the surviving spouse inherits the decedent's entire net estate. Wis. Stat. § 852.01(1)(a)1. This occurs regardless of the classification of the assets subject to probate administration.

## **C. Decedent Leaves Surviving Spouse and Issue; All Issue Are of Surviving Spouse and Decedent**

### **[§ 12.18]**

If the decedent leaves a surviving spouse and one or more issue and all issue are of the decedent and the surviving spouse, the surviving spouse inherits the decedent's entire net estate regardless of its classification. Wis. Stat. § 852.01(1)(a)1. The net estate consists of the decedent's one-half interest in former marital property, entire interest in former individual property, and entire interest in predetermination date property. The surviving spouse already owns a one-half interest in the former marital property assets subject to administration.

The net estate does not contain the decedent's interest in nonprobate assets such as joint tenancy and life insurance proceeds because they are not subject to administration. With respect to assets not subject to administration, the surviving spouse may make the deferred marital property election provided for by section 861.02. *See infra* §§ 12.136–.147.

### **D. Decedent Leaves Surviving Spouse and Issue; One or More Issue Are Not of Surviving Spouse and Decedent [§ 12.19]**

If the decedent leaves a surviving spouse and issue and one or more of the issue are not the surviving spouse's issue, the surviving spouse receives half of the decedent's estate subject to administration other than marital property, and the issue receive the balance of the decedent's estate. Wis. Stat. § 852.01(1)(a)2., (b). The surviving spouse may make the deferred marital property election with respect to assets not subject to administration. Wis. Stat. § 861.02; *see infra* §§ 12.136–.147; *Carroll v. Ansley (In re Estate of Carroll)*, 2001 WI App 120, 244 Wis. 2d 280, 628 N.W.2d 411.

## **V. Wills [§ 12.20]**

### **A. In General [§ 12.21]**

Chapter 853 governs the execution and effect of wills. A married decedent's will is effective to transfer all the decedent's interest in property subject to administration. *See supra* §§ 12.4–.11.

### **B. Equitable Election [§ 12.22]**

#### **1. In General [§ 12.23]**

The doctrine of equitable election exists in Wisconsin. Wis. Stat. § 853.15; *Schaech v. Schaech (Will of Schaech)*, 252 Wis. 299, 31 N.W.2d 614 (1948). In general, the doctrine applies if the testator attempts to dispose by will of assets that belong to a beneficiary of the will. If the doctrine applies, the will beneficiary is required to choose between the benefits under the will and the assets that the testator is attempting to transfer. In such cases, the beneficiary must forfeit benefits under the will if the beneficiary decides to retain ownership of the assets that the testator attempted to transfer.

The doctrine of equitable election applies more frequently since the Act was adopted because the maker of the will may believe that he or she

owns an entire asset when, in reality, it is marital property or deferred marital property.

## 2. The Statute [§ 12.24]

Section 853.15(1) provides in part as follows:

(1) Necessity for Election. (a) *Unless the will provides otherwise*, this subsection applies if a will gives a devise to one beneficiary and also clearly purports to give to another beneficiary property that does not pass under the will but belongs to the first beneficiary by right of ownership, survivorship, beneficiary designation or otherwise.

(b) If the conditions in par. (a) are fulfilled, the first beneficiary must elect either to take under the will and transfer his or her property in accordance with the will or to retain his or her property and not take under the will. If the first beneficiary elects not to take under the will, *unless the will provides otherwise* his or her devise under the will shall be assigned to the other beneficiary.

(c) This section does not require an election if the property belongs to the first beneficiary because of transfer or beneficiary designation made by the decedent after the execution of the will.

(Emphasis added.) The italicized portions of the statute quoted above indicate that the maker of the will may indicate in the will whether or not the doctrine of equitable election is to apply.

➤ **Note.** The 1985 Trailer Bill amended the statute so that election of the deferred marital property share under section 861.02 could trigger the equitable election. 1997 Wisconsin Act 188 changed the election from the right to elect a fractional interest to the right to elect an amount. Since the surviving spouse cannot elect an ownership interest in assets, section 853.15(1) was amended to delete the deferred marital property election as a trigger of the equitable election. 1997 Wis. Act 188, § 142.

## 3. Examples [§ 12.25]

➤ **Example 1.** A husband owned and operated a closely held corporation, XYZ, Inc., before and after the determination date. The stock of the corporation has always been titled in the husband's name. The husband has children who are now active in the business. Other

assets are also titled in the husband's name. The stock and all other assets held by the husband are marital property or individual property. The husband has a will that provides the following: "I leave all the outstanding shares of stock in XYZ, Inc., to my children in equal shares, and I leave the residue of my estate to my spouse if my spouse survives me, otherwise to the children."

The husband predeceases his wife. Assume the full value of the stock titled in the husband's name is \$300,000 and the full value of the other assets titled in the husband's name is \$300,000. Also, assume that one-half of each asset is marital property and the other half of each asset is the husband's individual property. The husband's gross estate is \$450,000: marital property of \$150,000 and individual property of 300,000.

H		W
Stock	75,000	75,000
Stock	150,000	
Other	75,000	75,000
Other	150,000 <sup>1</sup>	
Total		150,000 <sup>2</sup>
Estate	450,000	

<sup>1</sup> Take \$150,000

<sup>2</sup> Keep right column

The will can be interpreted in either of two ways. The first interpretation is that the husband's interest in the stock (his marital property interest of \$75,000 plus his \$150,000 interest in the balance of the stock, for a total of \$225,000) is left to the children and the residue (his \$75,000 marital property interest in the other assets and his \$150,000 interest in the balance of the other assets, for a total of \$225,000) is left to the spouse. This is not what the testator intended.

The second interpretation is that the will puts the surviving spouse to an equitable election under section 853.15. Under the doctrine of equitable election, if the predeceasing spouse attempts to dispose of an asset owned by the surviving spouse (in this case, a marital property interest in the stock), the surviving spouse is required to elect

1. To accept the benefits under the will and consent to the predeceasing spouse's disposition of the asset; or
2. To reject the benefits of the will and retain the asset.

Section 853.15(1)(a) provides that a will should require an election only if it "clearly purports" to dispose of the property. Therefore, if the will may be construed as attempting to dispose of the surviving spouse's one-half interest in marital property, a factual determination must be made whether the doctrine of equitable election applies.

In the above example, if the doctrine of equitable election applies, the wife must elect either to take under the will (which would involve the other assets) and transfer her marital property interest in the stock to the children or to retain her marital property interest in the stock and other assets and forfeit any benefits under the will.

If the doctrine of equitable election applies in the example, the wife can choose between two elections. First, she can affirm the will, take the residue (\$225,000), and transfer her interest in the stock (\$75,000) to the children. This is the result the testator intended. The children get all the stock, and the spouse gets all the other assets. Second, the spouse can elect not to take under the will and keep her marital property interest in the stock (\$75,000) and her marital property interest in the other assets (\$75,000). If the wife makes the equitable election against the will, she ultimately owns \$75,000 plus \$75,000 for a total of \$150,000.

The wife will probably not reject the will.

➤ **Example 2.** The full value of a duplex inherited by a wife from her mother is \$50,000. The full value of the residue of the wife's estate is \$200,000. Assume that the duplex is marital property because of the application of the mixing rules contained in section 766.63. Assume that the residue is individual property. The will contains the following provision: "I leave the duplex that I inherited from my mother to my son, John, by my first marriage. I leave the residue of my estate to my second husband."

H	W
Duplex 25,000	25,000
Residue	200,000

Is the husband put to an election under section 853.15? There is very little guidance as to when the will “clearly purports” to dispose of the surviving spouse’s interest in property within the meaning of section 853.15(1)(a). If the husband is not put to an election, he may retain his marital property interest in the duplex (\$25,000) and receive all the residue, for a total of \$225,000. If the husband is put to an election, he must elect between his marital property interest in the duplex (\$25,000) and the residue (\$200,000). Section 853.15(1)(a) does not take values into account.

➤ **Practice Tip.** The complications of the doctrine of equitable election illustrate the importance of understanding the classification of assets at the time the will is executed. A marital property agreement can be very helpful in clarifying classification. It is necessary to consider whether the doctrine of equitable election has been invoked; the procedural requirements in section 853.15(2) may apply even if one is unaware that they apply.

#### 4. Procedure [§ 12.26]

Section 853.15(2) provides that *if an election is required*, the following provisions apply:

1. The court may, by order, set a time within which the beneficiary must file with the court a written election either to take under the will and forgo, waive, or transfer his or her property interest in favor of the person to whom it is given by the will or to retain the property interest and not take under the will. Wis. Stat. § 853.15(2)(a). The time set must be no earlier than one month after the necessity for such an election and the nature of the interest given to the beneficiary under the will have been determined. *Id.*
2. If a written election to take under the will has not been filed with the court within the time set by order, *or if no order setting a time has*



*been entered* before final judgment, the beneficiary is deemed to have elected not to take under the will. Wis. Stat. § 853.15(2)(b).

➤ **Comment.** The procedure for making an equitable election is very rigid and can result in adverse consequences. For example, assume that the will puts the surviving spouse to an equitable election and the surviving spouse is unaware of that fact. Under section 853.15(2)(b), the surviving spouse is deemed to have elected against the will, so the surviving spouse forfeits all benefits under the will. Alternatively, assume that the surviving spouse is not sure whether he or she has been put to an equitable election. In this instance, the surviving spouse should consider requesting the court to determine whether the equitable election has been triggered, and if it has, should consider requesting the court to set the time within which the election must be made.

➤ **Practice Tip.** The personal representative may wish to consider bringing on a hearing regarding equitable election. This would avoid problems that may arise subsequently if the court never sets the time for making the election, with the result that the surviving spouse is deemed to have elected against the will.

## VI. Powers and Duties of Personal Representatives

### [§ 12.27]

#### A. Management and Control [§ 12.28]

##### 1. In General [§ 12.29]

During administration, the management and control rules under section 766.51 apply to a married decedent's property that is subject to administration and to the surviving spouse's property. Wis. Stat. § 857.01. If the surviving spouse makes the deferred marital property election, *see infra* §§ 12.136–.147, the personal representative may manage and control the property elected while the property is subject to administration. Wis. Stat. § 857.01. The management and control rules of the Act are described in chapter 4, *supra*.

## **2. Manner in Which Assets Titled or Held [§ 12.30]**

### **a. Assets Titled or Held Solely in Decedent Spouse's Name [§ 12.31]**

When one spouse dies, predetermination date property or individual property subject to probate administration may be titled solely in the name of the deceased spouse. Marital property assets may also be held in the name of the deceased spouse. In any case, the authority of the personal representative to manage all such property is free of doubt. If the asset is predetermination date property or individual property and is titled solely in the decedent's name, the personal representative owns the property and has the authority to manage it. Wis. Stat. §§ 766.51(1)(a), 857.01. If the asset is marital property or has a marital property component and is held solely in the decedent's name, the personal representative has authority to manage the entire asset, Wis. Stat. §§ 766.51(1)(am), 857.01, but owns only an undivided one-half interest in the former marital property, Wis. Stat. § 861.01(1).

Section 766.31(3)(b) permits divisions of marital property on an aggregate rather than on an item-by-item basis. For a general discussion of this provision, see section 2.22, *supra*. For a discussion of the federal and Wisconsin tax issues relative to this change, see section 9.20, *supra*. For suggested provisions to include in a marital property agreement to accommodate this change, see section 7.151, *supra*.

### **b. Assets Titled or Held in Both Spouses' Names [§ 12.32]**

Usually, if predetermination date property subject to probate administration is titled in both spouses' names, the personal representative and the surviving spouse must manage the asset together. However, some accounts expressly permit management by either party. Likewise, if an asset that is individual property is titled in both spouses' names (for example, tenancy-in-common property), the personal representative and surviving spouse must usually manage the asset together. Some accounts expressly permit management by either party.

If marital property assets are held in both spouses' names in the "and" form, the personal representative and the surviving spouse must both

manage the asset. Wis. Stat. § 766.51(2). If an asset is 100% marital property and is held in the “or” form, it may be managed by either the personal representative or the surviving spouse. Wis. Stat. § 766.51(1)(b); *see also supra* § 2.249. If an asset is mixed property—that is, partly marital and partly nonmarital—and the asset is held in the “or” form, it must be managed by both the personal representative and the surviving spouse because of the rules applicable to the nonmarital portion.

Section 766.31(3)(b) permits divisions of marital property on an aggregate rather than on an item-by-item basis. For a general discussion of this provision, see section 2.22, *supra*. For a discussion of the federal and Wisconsin tax issues relative to this change, see section 9.20, *supra*. For suggested provisions to include in a marital property agreement to accommodate this change, see section 7.151, *supra*.

### **c. Assets Titled or Held Solely in Surviving Spouse’s Name [§ 12.33]**

Assets that are titled or held solely in the name of the surviving spouse may be the surviving spouse’s predetermination date property, the surviving spouse’s individual property, or former marital property. Since assets titled or held solely in the surviving spouse’s name may be former marital property or have a former marital property component, the personal representative must ascertain whether the surviving spouse is holding former marital property. If so, the estate’s interest in the former marital property assets is subject to administration and must be reflected on the personal representative’s inventory and accounts, even though the surviving spouse has the exclusive right to manage the property.

➤ **Practice Tip.** The personal representative should consider causing the personal representative’s name to be added to the title for management and control purposes. Liability can result from the manner in which an asset is managed during administration.

Section 766.31(3)(b) permits divisions of marital property on an aggregate rather than on an item-by-item basis. For a general discussion of this provision, see section 2.22, *supra*. For a discussion of the federal and Wisconsin tax issues relative to this change, see section 9.20, *supra*.

For suggested provisions to include in a marital property agreement to accommodate this change, see section 7.151, *supra*.

**d. Assets Titled or Held in Third Person's Name**  
**[§ 12.34]**

Assets that are not titled or held solely by the decedent or the surviving spouse may be held or titled in the name of a third person. For example, one spouse may die when there are assets in a revocable living trust held by an independent trustee. Some or all of the assets in the trust may be marital property or have a marital property component, which normally is subject to administration. However, the trustee is authorized to manage the assets under the trust instrument's terms. Wis. Stat. § 766.51(3). The personal representative may have to work out the details of management with the trustee.

**3. Petitions for Relief with Respect to Management and Control [§ 12.35]**

Section 857.01 permits the personal representative or surviving spouse to petition the court for an order providing the equitable relief necessary for the management and control of marital property during the administration of an estate. Therefore, if former marital property assets are held solely in the name of the surviving spouse, the personal representative may petition the probate court for an order requiring either that the former marital property assets be titled in the names of the personal representative and the surviving spouse as tenants in common or that the property be divided. The statute permits many possibilities, including the following:

1. If the asset is reregistered, the new title could be registered as "XYZ Bank, as personal representative of the estate of John Jones, deceased, and Mary Jones, as tenants in common of an undivided one-half interest each."
2. The asset could be divided, with one-half registered solely in the personal representative's name and the other half registered solely in the surviving spouse's name.

3. The asset could be registered in one name, either the personal representative's or the surviving spouse's.

An asset might not be entirely marital property; it might be mixed property. In that case, the personal representative and the surviving spouse are tenants in common, but their fractional interests are not each 50%. If an asset is 70% marital property, the balance was nonmarital property owned by the decedent spouse, the asset was not partitioned, and the new registration is in both names, the new registration could read, "XYZ Bank, as personal representative of the estate of John Jones and Mary Jones, as tenants in common, XYZ Bank having a 65% undivided interest and Mary Jones having a 35% undivided interest."

#### 4. Statutory Buy-Sell Procedure [§ 12.36]

If a decedent spouse held an interest in a partnership or closely held corporation, the personal representative must determine whether the decedent executed a directive under section 857.015 necessitating a mandatory exchange under sections 766.51(10) and 861.015. Together, these sections create a statutory buy-sell procedure. The personal representative may be involved in two ways:

1. If the decedent did execute a written directive, the personal representative is obligated to carry it out. The personal representative must satisfy the surviving spouse's marital property interest in the designated property within one year of death. Wis. Stat. § 861.015(1). The surviving spouse's interest may be satisfied from other property that is of equal clear market value at the time of satisfaction. *Id.*
2. If the decedent did not execute a written directive, the personal representative may not execute a directive on the decedent's behalf. Wis. Stat. § 857.015.

➤ **Note.** If the surviving spouse is the holding spouse, he or she may execute a written directive within 90 days of the decedent's death. *Id.* Since 90 days is a short period, the personal representative may wish to consider advising the surviving spouse to seek separate counsel regarding the written directive.

➤ **Note.** The statutory buy-sell provision applies to both marital property assets and deferred marital property. However, with the change of the deferred marital property election to an amount instead of a fractional interest in individual assets, use of the statutory buy-sell procedure is no longer necessary with respect to deferred marital property. If the surviving spouse makes the deferred marital property election, the spouse receives cash. See section 4.81, *supra*, for an additional discussion of the statutory buy-sell provision.

## **B. Classification of Assets [§ 12.37]**

### **1. Classification Presumptions During Administration [§ 12.38]**

The presumption contained in section 766.31(2), that all assets are presumed to be marital property, applies during administration of a decedent's estate. Wis. Stat. § 854.17.

If the marital property presumption is rebutted, a second presumption applies. Section 861.02(2)(a) provides that if the presumption under section 766.31(2) is overcome, the property is presumed to be deferred marital property.

Therefore, there are two presumptions during administration of a decedent's estate. All assets, whether titled or held in the name of the decedent spouse, the surviving spouse, or both spouses, are presumed to be marital property. If the marital property presumption is overcome, predetermination date property owned by the decedent spouse is presumed to be deferred marital property. If the second presumption is overcome, the property is not classified as former marital property, and the surviving spouse has no deferred marital property election because the property is not deferred marital property.

➤ **Example.** A decedent spouse inherited IBM stock in 1976 during marriage. The stock was registered in the name of the decedent spouse. The certificate was dated April 1, 1976. In 1998, the decedent spouse sold the IBM stock and used the proceeds to purchase AT&T stock. The new stock certificate is dated April 1, 1998.

How is the stock classified for purposes of administration? First, the stock is presumed to be marital property. Records may be available to show that the AT&T stock is traceable to nonmarital property, thus overcoming the presumption. If the presumption is not overcome, the stock is classified as marital property stock. Assume that the personal representative can show that the AT&T stock was purchased with the proceeds from the sale of the IBM stock. Since the IBM stock certificate was dated April 1, 1976, the IBM stock was predetermination date property. Predetermination date property cannot be marital property, so the first presumption is overcome. However, the second presumption now applies. The IBM stock is presumed to be deferred marital property. To overcome the second presumption, the personal representative must show that the IBM stock was acquired by gift or disposition at death. If the second presumption is not overcome, the AT&T stock is deferred marital property and is in the augmented deferred marital property estate, and the surviving spouse has the right to make the deferred marital property election under section 861.02. *See infra* §§ 12.136–.147 (deferred marital property election), .148–.162 (augmented deferred marital property estate).

## **2. Manner in Which Assets Titled or Held [§ 12.39]**

### **a. Classification of Assets Titled or Held Solely in Decedent Spouse's Name [§ 12.40]**

Assets that are titled or held solely in the decedent spouse's name may be the decedent's predetermination date property, the decedent's individual property, or marital property of the spouses. An asset may also be mixed property—that is, a mixture of marital property and nonmarital property—if the nonmarital property component can be traced. Wis. Stat. § 766.63.

If an asset titled or held solely in the decedent spouse's name is marital property or has a marital property component, the personal representative and surviving spouse are tenants in common with respect to the former marital property. Wis. Stat. § 861.01(2).

**b. Assets Titled or Held in Both Spouses' Names**  
**[§ 12.41]**

If an asset is titled or held in both spouses' names, the asset is co-owned. If predetermination date property or individual property is co-owned and subject to administration, it is tenancy-in-common property. The personal representative owns a fractional ownership interest in the property. If the property was marital property, it becomes tenancy-in-common property upon the death of the first spouse to die. Wis. Stat. § 861.01(2).

**c. Assets Titled or Held Solely in Surviving Spouse's Name [§ 12.42]**

Assets titled or held solely in the surviving spouse's name may be marital property or have a marital property component. If so, the personal representative and the surviving spouse are tenants in common as to the former marital property. Wis. Stat. § 861.01(2). Since the asset is titled or held solely in the surviving spouse's name, the surviving spouse has the sole authority to manage and control the asset. Wis. Stat. §§ 861.01(1), 857.01. However, the personal representative's ownership interest is subject to administration.

The personal representative must ascertain the classification of all assets that are either titled in the surviving spouse's name or untitled and in the surviving spouse's possession. Such assets may be marital property or have a marital property component. If so, the decedent's interest is subject to administration. The burden of proof that the asset is not marital property is on the surviving spouse. Wis. Stat. §§ 854.17, 861.02(2)(a).

If the surviving spouse makes the deferred marital property election, it is necessary to determine whether any assets titled or held solely in the surviving spouse's name are deferred marital property. *See infra* §§ 12.156–.159.



## **d. Assets Titled or Held in Trustee's Name**

### **[§ 12.43]**

#### **(1) In General [§ 12.44]**

A spouse may die while marital property assets are owned by the trustee of a revocable living trust. Sections 12.45–.47, *infra*, discuss (1) issues that arise when the sole settlor spouse dies first, (2) issues that arise when the nonsettlor spouse dies first, and (3) tax consequences of holding marital property assets in a revocable trust.

#### **(2) Sole Settlor Spouse Dies First [§ 12.45]**

If the sole settlor of a revocable living trust dies survived by the other spouse, the trust becomes irrevocable by reason of the settlor's death. Under section 861.01, the surviving spouse (a nonsettlor) owns a one-half interest in any former marital property assets as a tenant in common with the trustee. If the trust instrument provides for the disposition of the surviving spouse's marital property interest, the trustee should comply with the direction for disposition.

If the trust instrument does not provide for a disposition of the surviving spouse's one-half marital property interest upon the death of the settlor spouse, the trustee has the authority to manage the surviving spouse's one-half tenancy-in-common interest. Section 766.51(3) provides that the right to manage and control marital property transferred to a trust is determined by the trust's terms. Presumably, if the trustee holds marital property, section 766.51(3) continues to apply when the marital property ceases being marital property, as it would when one spouse dies. Section 766.575(2) provides that the "classification" of property in the trust does not affect the trustee's right and duty to administer, manage, and distribute the trust property. Again, presumably, if marital property is converted to tenancy-in-common property by reason of a spouse's death, the statute continues to apply even though, technically, the marital property assets are no longer classified when they become tenancy-in-common assets upon the death of one spouse.

Section 766.575(4) provides that a trustee is not liable to any person for any claim for damages as a result of a distribution of property in

accordance with the terms of the governing instrument before the trustee's receipt of a notice of claim under section 766.575(3).

➤ **Comment.** The longer the trustee continues to hold the surviving spouse's one-half tenancy-in-common interest, the more complicated the situation may become. At some point, it may be argued that the predeceasing settlor spouse has made a nonprobate transfer of marital property assets to the beneficiaries of the revocable living trust. Section 766.70(6)(b)1. provides that in the event of a nonprobate transfer of marital property assets to a third person, the surviving spouse may bring an action against the third person to recover one-half of the marital property assets transferred. The surviving spouse may not commence such an action later than one year after the death of the decedent spouse. Wis. Stat. § 766.70(6)(b)1.; *see supra* § 12.12. If the statute of limitation expires, the surviving spouse may have no means of recovering the former marital property assets, *see supra* ch. 8, and a gift for tax purposes may result, *see supra* ch. 9.

➤ **Practice Tip.** Given the complexity of the issues that may arise upon the death of a spouse when a trust holds marital property assets, the trust instrument should contain provisions alerting the trustee to the potential situation and creating a procedure for dealing with the situation. Provisions for the distribution of marital property interests are discussed in chapter 10, *supra*. In many cases, using a joint revocable living trust agreement is preferable to a trust with one settlor because the issues are more likely to come to light.

### (3) Nonsettlor Spouse Dies First [§ 12.46]

Section 12.45, *supra*, describes the situation that may exist if the settlor of a revocable living trust dies survived by a spouse and the trust holds marital property assets or income. A similar situation exists if the nonsettlor spouse dies survived by the settlor spouse.

If a personal representative has been appointed for the decedent nonsettlor spouse, as long as the predeceasing spouse's estate is open, it appears that the personal representative can recover the decedent's one-half interest in former marital property assets that are now tenancy-in-common assets. It appears that the personal representative has the option of either recovering the one-half interest or simply permitting the one-half interest to remain in the trust subject to administration by the probate

court and management by the trustee. Of course, the personal representative's right to recover can be enforced at any time.

If administration of the decedent's estate is formal administration and a final judgment is entered assigning all the decedent's assets, it would appear the final judgment would transfer the decedent's interest in the trust. If the administration is informal administration, no transfer would have occurred since transfers in informal administration occur by express assignment executed by the personal representative. There is no general statute of limitation regarding the expiration of the decedent's ownership in the trust assets.

➤ **Comment.** This is a situation showing the advantage of a formal administration over an informal administration—namely, finality regarding decisions made determining ownership of assets.

#### **(4) Tax Consequences of Holding Marital Property Assets in Revocable Trust [§ 12.47]**

If the settlor dies survived by the other spouse and the trust contains marital property assets that are generating income, the income from the deceased settlor's interest is reported for tax purposes as the income of an irrevocable trust. The income from the surviving spouse's interest is reported as the income of a grantor trust.

If the nonsettlor spouse dies survived by the settlor, the income from the decedent's portion of the trust is reported as income of the decedent's estate, and the income from the surviving settlor's portion is reported as the income of a grantor trust. *See supra* ch. 9 (taxation of revocable trusts).

If a revocable living trust holds marital property assets and the settlor spouse predeceases the other spouse, a taxable gift may result if the surviving spouse fails to withdraw his or her interest in former marital property assets from the trust. *See* Wis. Stat. §§ 766.53, .70(6). This gift may be a gift of a future interest and may therefore be ineligible for the federal annual gift tax exclusion under I.R.C. § 2503. As to when gifts take place for gift tax return filing requirements, see chapter 9, *supra*.

With respect to the federal estate tax, a transfer of marital property assets to a revocable trust does not by itself change the classification of the property in the trust. Wis. Stat. § 766.31(5). If one spouse predeceases the other, the predeceasing spouse's one-half interest in the marital property assets in the trust will be included in his or her gross estate under I.R.C. § 2033.

One of the most important considerations when marital property assets are in a revocable trust is whether they retain their classification for purposes of the full-adjustment-in-basis rule of I.R.C. § 1014(b)(6). As noted above, a transfer of marital property assets to a revocable living trust does not by itself change the classification of the assets. Wis. Stat. § 766.31(5). Assuming that nothing in the trust instrument would change the classification, assets held by the trust receive the full adjustment in basis on the death of the first spouse to die. Rev. Rul. 66-283, 1966-2 C.B. 297.

### **3. Rebutting the Presumption [§ 12.48]**

Practices will evolve for rebutting the presumption that property is marital property or deferred marital property. *See supra* ch. 3. If the decedent's will leaves everything to the surviving spouse or if the surviving spouse inherits the entire estate through intestacy, classification will not be as important as it would be if the decedent's will left assets to someone other than the surviving spouse (e.g., a trust, children, or a charity). If the decedent's will leaves everything to the surviving spouse, the extent of the efforts that the personal representative must apply to rebut the presumption of marital property is unknown. If the personal representative permits the marital property presumption to apply, the personal representative's fee and inventory filing fee may be reduced because the value of property subject to administration is reduced. Wis. Stat. §§ 857.05, 814.66. There is a potential income tax advantage to marital property—namely, the full adjustment in basis. *See supra* § 9.22.

### **4. Petitions Regarding Classification of Property [§ 12.49]**

Depending on the situation, the personal representative or the surviving spouse may need to petition the probate court, as authorized by

section 857.01, for an order determining the classification of certain assets.

➤ **Example.** A wife inherited stock worth \$10,000 when her mother died in 1976. Thereafter, the wife sold some of the stock, reinvested some of the proceeds, spent some of the proceeds, made additions to the portfolio from her wages, and reinvested some of the dividends. She did not maintain adequate records. Her actions occurred before and after the determination date. The wife's will leaves the stock to her children by a prior marriage for their college educations. The husband dies first. His will leaves his estate to his children by a prior marriage. The value of the stock fund is \$25,000 on the husband's death.

It must be determined whether the husband has a marital property interest in the stock fund. The stock fund appears to be hopelessly mixed to the extent that original certificates no longer exist. If so, the presumption that the securities are marital property cannot be overcome. If the presumption is not overcome, the personal representative must take the position that the stock is marital property. Depending on the circumstances, the personal representative may need to petition the court for an order determining classification. A petition would give all parties concerned an opportunity to be heard regarding the classification of the stock fund.

In the above example, the surviving spouse may be the personal representative. If so, the surviving spouse may have a conflict of interest. *See infra* § 12.51.

## **5. Traceable Mixing: Ownership vs. Right of Reimbursement [§ 12.50]**

Section 766.63(1) provides that, except as provided otherwise in section 766.61 (life insurance) and section 766.62 (deferred employment benefits), mixing marital property with nonmarital property reclassifies the nonmarital property to marital property unless the nonmarital property can be traced. The court of appeals has held that when mixing is traceable, the surviving spouse has a right of reimbursement, not an ownership interest, in the mixed asset. *Kobylski v. Hellstern (In re Estate of Kobylski)*, 178 Wis. 2d 158, 503 N.W.2d 369 (Ct. App. 1993).

So, for example, if the decedent owned nonmarital real estate subject to traceable mixing, the personal representative must classify the real estate as nonmarital property on the inventory. If the surviving spouse intended the mixing to be a gift to the decedent, the remedies for gift recoveries are available. If the surviving spouse did not intend a gift, the surviving spouse has a claim for reimbursement, which must be filed pursuant to section 859.01. *See infra* §§ 12.124–.128.

### C. Conflicts of Interest [§ 12.51]

Lawyers who advise personal representatives and surviving spouses may have potential and actual conflicts of interest. For further discussion, see chapter 14, *infra*.

Potential or actual conflicts of interest may also exist between the personal representative and the surviving spouse. If there is a potential or actual conflict of interest between the duties of the personal representative and the interests of the surviving spouse, it may be that the surviving spouse should not serve as personal representative. The probate court has inherent power to refuse to appoint the surviving spouse as personal representative, even though nominated by the decedent, or to remove the surviving spouse if the surviving spouse has already been appointed. *Oak Park Trust & Savings Bank v. Tressing (In re Estate of Tressing)*, 86 Wis. 2d 502, 273 N.W.2d 271 (1979); *see also Keske v. Marshall & Ilsley Bank (In re Estate of Keske)*, 18 Wis. 2d 47, 117 N.W.2d 575 (1962).

A number of circumstances may trigger situations in which there is a potential or actual conflict of interest between the surviving spouse and the personal representative. Areas of potential conflict of interest include:

1. Classification of property when the surviving spouse is not the sole beneficiary of the estate;
2. The right to make the deferred marital property election;
3. Advice concerning the deferred marital property election;

➤ **Note.** In *Schadde v. Estate of Schadde*, No. 90-0542-FT, 1991 WL 97310 (Wis. Ct. App. Apr. 25, 1991) (unpublished opinion

not citable per section 809.23(3)), the court held that the personal representative does not have a duty to inform the surviving spouse of the six-month deadline for filing the deferred marital property election, citing *Ludington v. Patton*, 111 Wis. 208, 230, 86 N.W. 571 (1901).

4. Decisions on whether the marital property presumption and deferred marital property presumption can be rebutted;
5. Enforceability of marriage agreements, marital property agreements, unilateral statements, and written consents;
6. Decisions on whether actions for recovery of marital property or breach of the good-faith duty under section 766.70 should be commenced;
7. Determination of whether the will puts the surviving spouse to an equitable election; and
8. Satisfaction of obligations and expenses of administration.

#### **D. Apportioning Expenses of Administration Between Marital and Nonmarital Property [§ 12.52]**

##### **1. The Statute [§ 12.53]**

Section 857.04 provides as follows:

**Distribution of Marital and Other Expenses.** (1) Except as provided in sub. (2), the personal representative shall pay expenses of administration out of the decedent's interests in marital property and in property other than marital property on a prorated basis according to the value of those interests.

(2) To the extent possible, the personal representative shall pay special expenses attributable to the management and control of marital property from the marital property generating the expenses, and special expenses attributable to the management and control of the decedent's property other than marital property from the other property generating the expenses.

## 2. General Expenses of Administration [§ 12.54]

Section 857.04(1) directs the personal representative to pay expenses of administration out of the decedent's interests in marital property and nonmarital property on a prorated basis. This book refers to these expenses as *general expenses of administration*.

➤ **Example.** A decedent's interests in marital probate property are valued at \$50,000, and the decedent's interests in nonmarital probate property are valued at \$50,000. The total estate is \$100,000. General expenses of administration are \$2,000.

Section 857.04(1) requires the personal representative to pay one-half of the general expenses of administration from the decedent's interest in marital property and the other half of the general expenses of administration from the nonmarital property. The statute does not distinguish specific bequests and devises from residue.

A number of practical questions arise from section 857.04(1). First, assume that a will leaves everything to the surviving spouse. Is it necessary to apportion expenses as dictated by section 857.04(1)? Under a literal reading of the statute, the decedent's marital property interests must be determined and valued. After classification and valuation, administration expenses must be prorated between the marital property and the nonmarital property. However, if the surviving spouse is receiving the entire estate anyway, apportioning expenses should not be necessary. Second, assume that the will provides for a \$5,000 pecuniary bequest to a child. Does the pecuniary bequest bear any portion of the general expenses of administration? Presumably not, otherwise the legatee would not receive \$5,000. In addition, section 857.04(1) charges a portion of the expenses of administration to marital property, without specifying the apportionment of the expenses within the classification. Section 854.18, which deals with abatement, apportions expenses within classifications. Third, assume that the will leaves a specific bequest of stock to a child. Must expenses of administration be charged to the stock? Presumably not, because otherwise the child would not receive all the stock. In addition, as with pecuniary bequests, the abatement section, section 854.18, appears to apportion expenses within classifications of property. Section 857.04(1) does not require apportionment of administration expenses on an asset-by-asset basis within a classification. Fourth, what if an asset is not liquid? Read



literally, the statute does not make any exceptions for illiquidity. Must illiquid assets be sold? A sale might produce a harsh result, depending on the circumstances.

In the absence of legislative clarification, the following is offered as a way to harmonize the various ambiguities regarding section 857.04(1). Section 854.18 provides an order in which assets abate to pay expenses of administration. Section 854.18 controls within a classification. Therefore, expenses of administration are payable out of the residue of each classification to the extent that the residue is sufficient.

The application of section 857.04(1) may require a court order in certain circumstances. If informal administration is being used, it may be necessary to switch to formal administration temporarily.

➤ **Practice Tip.** The statute is silent on whether the decedent's will can negate the application of section 857.04. However, there is certainly no harm in putting a clause in the will attempting to negate section 857.04(1). At the very least, such a clause would support a court order. See section 10.185, *supra*, for a form giving the personal representative discretion to apportion administration expenses.

Likewise, it is unknown whether the probate court can change the effect of section 857.04. However, probate courts are courts of equity. Presumably, the court's equitable powers would permit the court to alter the effect of section 857.04(1) when warranted by the circumstances.

### **3. Special Expenses of Administration [§ 12.55]**

Section 857.04(2) provides that to the extent possible the personal representative is to prorate special expenses attributable to management and control between marital property and nonmarital property. Unlike section 857.04(1), section 857.04(2) does not refer to the decedent's interest in marital property. Section 857.04(2) refers to marital property, which presumably includes the interests of both spouses. Also, unlike section 857.04(1), which refers to a classification of property, section 857.04(2) refers to a particular asset. Whether the asset is residue or not appears to make no difference.

➤ **Example.** Assume that a husband solely held a duplex, which was marital property. The husband dies. The husband's will specifically devises his interest in the duplex to his wife. The personal representative and the wife decide that the personal representative will manage the duplex. Special expenses of administration relating to the management and control of the duplex are prorated to the personal representative's one-half interest and the wife's one-half interest in the duplex.

Section 857.04(2) only applies "[t]o the extent possible" and does not distinguish between residue and specific bequests and devises. Presumably, if the particular asset being managed is not liquid, special expenses of administration are not charged to the asset because they cannot be charged unless the asset is sold. It remains an open question whether there is a right of reimbursement if the asset *is* sold.

If special expenses of administration are charged to the surviving spouse's one-half interest in former marital property, a portion of the deduction is lost for federal estate and Wisconsin inheritance tax purposes but may be an addition to basis. *See supra* ch. 9.

## **E. Notice of Adverse Claim to Third Parties [§ 12.56]**

The decedent's marital property interest may be in the hands of one or more third parties after the decedent's death. If so, the personal representative may consider either (1) giving a notice of adverse claim to the third party, to discourage the third party from transferring the decedent's property to someone else, or (2) requesting a court order, including a temporary restraining order, if necessary. Examples include the following:

1. The decedent may have had a "marital account" with the surviving spouse under section 705.01(4m). Section 705.06(1)(d) provides that after receipt of "actual notice" of the death of one party to a marital account, the financial institution may pay on request not more than 50% of the sums on deposit to the surviving party. Therefore, this section permits the financial institution to pay the entire balance in the marital account to the surviving party before "actual notice" is received. To prevent payment of the entire balance, the personal representative can give notice of the death to the financial institution.

2. The decedent may have had a marital property interest in a life insurance policy insuring the surviving spouse. Under section 766.61(2), the policy issuer is not liable for payments or actions taken unless, at the time of the payments or actions, it had actual knowledge of an inconsistent decree, marital property agreement, or adverse claim. If the life insurance company does pay the proceeds to someone other than the personal representative (e.g., the cash-surrender value is withdrawn), the personal representative has a remedy against the payee. Wis. Stat. § 766.70(6)(b).
3. The decedent may have had a marital property interest in a mutual fund, an account at a financial institution, or an account with a stock broker. If the account is titled in the surviving spouse's name, the personal representative may consider giving notice to the financial institution or stock broker in an attempt to prevent the third party from making payments to the surviving spouse. A question that may arise is whether the financial institution or stock broker is a bona fide purchaser under section 766.57. If so, notice of the existence of the marriage or termination of the marriage does not affect the status of the institution or broker as a bona fide purchaser under section 766.57(2).

## **F. Gift Recoveries [§ 12.57]**

### **1. Lifetime Gifts of Marital Property Assets by Decedent Spouse [§ 12.58]**

Section 766.70(6)(a) grants the surviving spouse a remedy if the decedent spouse, acting alone, gave marital property assets to a third person in excess of the limits set forth in section 766.53. The surviving spouse must commence the action for the remedy within the earlier of one year after he or she has notice of the gift, one year after a dissolution, or on or before the deadline for filing a claim under section 859.01 after the death of either spouse. *See* Wis. Stat. § 766.70(6)(a). Section 859.01 provides that all claims must be filed within a three- to four-month period commencing with the date that the order limiting time for filing claims is entered. Thus, assuming that the surviving spouse's remedy is not barred by the one-year limitation, the action by that spouse must be commenced during the three- to four-month limitation period or the expiration of the one-year period, if earlier.

➤ **Query.** Does the personal representative have a duty to advise the surviving spouse of this right? The better view is that the personal representative has no such duty. Rather than specifically advising the surviving spouse of this right and other rights, the personal representative may wish to advise the surviving spouse to have separate representation. That way, the personal representative would not be encouraging the exercise of specific rights the surviving spouse may have that may conflict with the personal representative's duty to the other beneficiaries. *See infra* ch. 14.

➤ **Note.** In *Schadde v. Estate of Schadde*, No. 90-0542-FT, 1991 WL 97310 (Wis. Ct. App. Apr. 25, 1991) (unpublished opinion not citable per section 809.23(3)), the court held that the personal representative does not have a duty to inform the surviving spouse of the six-month deadline for filing the deferred marital property election, citing *Ludington v. Patton*, 111 Wis. 208, 230, 86 N.W. 571 (1901).

## **2. Lifetime Gifts of Marital Property Assets by Surviving Spouse [§ 12.59]**

The surviving spouse, acting alone, may have made gifts of marital property assets to a third person in excess of the limits in section 766.53. If so, the personal representative must commence an action regarding the gift within the earlier of (1) one year after the decedent spouse had notice of the gift or (2) the three- to four-month filing time under section 859.01, if either spouse dies. *See* Wis. Stat. § 766.70(6)(a); *see also supra* § 12.58. Assuming that the action is not already barred under the notice provision, the personal representative must commence the action during the earlier of these two periods.

If a potential cause of action exists against the surviving spouse for gifts of marital property assets, the personal representative must consider several difficult matters, including the following:

1. The action is barred if not commenced after the decedent's death. The personal representative might want to investigate the possibility of gift recoveries.

2. A conflict of interest exists if the personal representative is the surviving spouse and residue passes to beneficiaries other than the surviving spouse. One solution is for the will to contain provisions permitting the surviving spouse to serve as personal representative despite conflicts of interest. The problem with such a provision in the will is that it is difficult to anticipate in advance all the conflicts of interest that may arise. Despite such a provision in the will, the probate court has inherent authority, if there is a conflict of interest, to refuse to appoint the surviving spouse or to remove the surviving spouse. *See supra* § 12.51.

➤ **Comment.** Apparently, an action against the surviving spouse for a recovery with respect to excessive gifts of marital property assets must be commenced in circuit court by a summons and complaint. Commencing an action in circuit court could lead to a delay in the probate proceedings. *See supra* § 8.45. Under section 766.70(6)(a), the personal representative may sue the surviving spouse and the donee. To commence the action, the personal representative must know the donee's identity. It may be difficult to discover the donee's identity within the three- to four-month filing period. Presumably, if a party is discovered after the action is commenced, the party can be added as a party defendant.

### **3. Right of Reimbursement as a Result of Traceable Mixing [§ 12.60]**

Section 766.63(1) provides that, except as provided otherwise in section 766.61 (life insurance) and section 766.62 (deferred employment benefits), mixing marital property with nonmarital property reclassifies the nonmarital property to marital property unless the nonmarital property can be traced. The court of appeals has held that when mixing is traceable, the surviving spouse has a right of reimbursement, not an ownership interest in the mixed asset. *Kobylski*, 178 Wis. 2d 158. So, for example, if the decedent owned nonmarital real estate subject to traceable mixing, ownership of the marital property funds has been transferred to the decedent. If the surviving spouse intended the mixing to be a gift to the decedent, the remedies for gift recoveries are available. If the surviving spouse did not intend a gift, the surviving spouse has a claim for reimbursement, which must be filed pursuant to section 859.01. See the discussion of claims at section 12.125, *infra*.

### G. Breach of Good-faith Duty [§ 12.61]

Section 766.15(1) requires each spouse to act in good faith with respect to the other spouse in matters involving marital property or other property of the other spouse. *See supra* § 8.18. If one spouse breaches the good-faith duty, the other spouse has a claim under section 766.70(1). Under section 766.70(1), a spouse has six years after acquiring actual knowledge of the facts giving rise to the claim in which to commence an action, except as limited in section 766.70(6). Section 766.70(6) contains the remedies for excessive gifts of marital property. Actions with respect to gifts of marital property have a shorter statute of limitation. *See supra* §§ 12.58–.59. Presumably, if a surviving spouse breached the good-faith duty and the decedent spouse, who owned the cause of action, died during the six-year limitation period, the personal representative succeeds to the decedent spouse's cause of action.

The decedent spouse may be the spouse who breached the good-faith duty. If so, the surviving spouse has a cause of action against the estate. This is another reason why the personal representative may wish to advise the surviving spouse to have separate representation. *See supra* § 12.58; *see also infra* ch. 14.

If the surviving spouse has a claim against the decedent spouse for breach of the good-faith duty and the claim sounds in tort, the claim is not subject to the three- to four-month claim period specified in section 859.01. If the claim does not sound in tort, however, it must apparently be filed within the section 859.01 claim period or it is barred, notwithstanding section 766.70(1).

Section 767.331 provides that no action under section 766.70 may be brought by a spouse against the other spouse while an action for divorce is pending. Some actions are section 766.70 actions and others are not. In *Gardner v. Gardner*, 175 Wis. 2d 420, 499 N.W.2d 266 (Ct. App. 1993), the court held that an action for intentional misrepresentation brought by the wife during the divorce proceeding was a section 766.70 action and the court therefore dismissed her case. In *Caulfield v. Caulfield*, 183 Wis. 2d 83, 515 N.W.2d 278 (Ct. App. 1994), the court held that an action for recovery on a note brought during the divorce proceeding was not a section 766.70 action.

In *Knafelc v. Dain Bosworth, Inc.*, 224 Wis. 2d 346, 591 N.W.2d 611 (Ct. App. 1999), the court held that an action by the wife against her stockbroker-husband regarding securities trades in the course of his employment was not a section 766.70 action. In *Stuart v. Stuart*, 140 Wis. 2d 455, 410 N.W.2d 632 (Ct. App. 1987), *aff'd*, 143 Wis. 2d 347, 421 N.W.2d 505 (1988), the ex-wife commenced a tort action after the judgment of divorce against her ex-husband for assault, battery, and intentional infliction of mental distress arising from incidents that allegedly took place during the marriage. The court of appeals and the supreme court upheld the ex-wife's action and held that a tort action for personal injury and divorce proceedings do not have an identity of causes of actions or claims.

## **H. Marital Property Agreements [§ 12.62]**

### **1. Obligations of Decedent Under Marital Property Agreement or Marriage Agreement [§ 12.63]**

One spouse may die having undertaken certain obligations in a marital property agreement or other marriage agreement. Unless the surviving spouse files a claim against the estate pursuant to section 859.01 or against a trust under section 701.065, the decedent's obligations are generally barred. The fact that the surviving spouse may have a claim against the estate or trust is another reason why the personal representative may wish to advise the surviving spouse to consider having separate representation. *See supra* § 12.58.

Section 766.58(13)(b) provides that no action on a marital property agreement may be brought later than six months after the inventory is filed. Section 766.58(13)(b) also contains provisions that apply when the inventory is amended. Section 766.58(13)(c) permits the court to extend the time for filing. Section 859.02(2)(a) provides that a claim based on a marital property agreement is generally subject to the limitations in subsections 766.58(13)(b) and (c).

➤ **Practice Tip.** Section 766.58(13)(b) applies to many situations not covered by section 859.02, which is limited to claims against the decedent's estate. Section 766.58(13)(b) would permit an action by the personal representative against the surviving spouse. It would also permit an action by the surviving spouse against the personal

representative for something that is not a claim against the decedent's estate—for example, a construction of a marital property agreement. The word *action* in section 766.58(13)(b) implies an action in circuit court commenced by summons and complaint. Also, section 766.58(13)(b) is not limited to use by the spouses or personal representative. It appears to apply to any action concerning a marital property agreement.

## **2. Breach of Marital Property Agreement or Marriage Agreement [§ 12.64]**

The decedent spouse or the surviving spouse may have breached a marital property agreement or other marriage agreement. Under section 766.58(13)(b), after the death of a spouse, no action concerning a marital property agreement may be brought later than six months after the inventory is filed. If an amended inventory is filed, the action may be brought within six months after the filing of the amended inventory, if the action relates to information contained in the amended inventory that was not contained in a previous inventory. Wis. Stat. § 766.58(13)(b). The court may extend the six-month period for cause if a motion for extension is made within the applicable six-month period. Wis. Stat. § 766.58(13)(c).

➤ **Note.** Section 766.58(13)(b) only applies to marital property agreements. A marriage agreement executed by spouses before their determination date may or may not be a marital property agreement. *See supra* ch. 7.

➤ **Note.** Probate is a series of special proceedings, not one proceeding. If a marital property agreement or marriage agreement is contested in the probate court and the court rules in favor of one party, the order is an appealable order. The rules for a timely appeal apply to that order. *Olson v. Dunbar (In re Estate of Olson)*, 149 Wis. 2d 213, 440 N.W.2d 792 (Ct. App. 1989) (holding that appeal from order upholding validity of agreement taken after final judgment in probate proceeding is not timely).



The considerations regarding breach of a marital property agreement or other agreement are similar to the matters that must be considered with respect to gift recoveries and breach of the good-faith duty discussed in sections 12.57–.60 and 12.61, *supra*, respectively.

See section 12.63, *supra*, for a discussion of the limitation periods described in sections 766.58(13)(b) and 859.02.

## **I. Life Insurance and Deferred-employment-benefit Plans [§ 12.65]**

### **1. Notice to Surviving Spouse of Life Insurance Policy or Deferred-employment-benefit Plan [§ 12.66]**

Section 857.35 states that if a personal representative who is not the surviving spouse becomes aware that any beneficiary other than the surviving spouse is designated as beneficiary of more than 50% of the proceeds of a life insurance policy or deferred-employment-benefit plan, the personal representative must give the surviving spouse written information sufficient to identify the policy or plan and its beneficiary. Section 857.35 also states that the surviving spouse may recover life insurance proceeds and deferred employment benefits under section 766.70(6).

Section 857.35 applies to all life insurance policies and all deferred-employment-benefit plans no matter how classified. Section 857.35 applies to all life insurance policies whether the insured is the decedent spouse or the surviving spouse. Presumably, the personal representative must give notice in every case to permit the surviving spouse to consider independently the classification of the asset and decide whether to assert a claim. If the proceeds are marital property and a claim is not asserted, a gift may result.

➤ **Caution.** The statute does not contain a time limit for notification. It simply states that the personal representative is obligated to notify the surviving spouse whenever the personal representative “becomes aware” that a third person was designated. By the time the personal representative becomes aware of such a beneficiary designation, the statute of limitation with respect to a

recovery by the surviving spouse may have expired. *See supra* §§ 12.57–.60.

## **2. Surviving Spouse's Option to Purchase Decedent's Interest in Life Insurance Policy or Deferred-employment-benefit Plan [§ 12.67]**

### **a. Life Insurance [§ 12.68]**

Section 766.70(7) states that after the date of death and within 90 days after the earlier of (1) receipt of the inventory listing any life insurance policy or deferred-employment-benefit plan or (2) the discovery of the existence of such a policy or plan, the surviving spouse may purchase the decedent's interest in the policy or plan from the decedent's estate at fair market value as of the date of death if all or part of the policy or plan is included in the decedent spouse's estate. Section 766.70(7) also states that it only applies to life insurance policies and deferred-employment-benefit plans described by sections 766.61 and 766.62.

Section 766.70(7) applies when the surviving spouse is the insured. The life insurance policy may be the individual property of the predeceasing spouse if, for example, the predeceasing spouse was the record owner of the policy. Wis. Stat. § 766.61(3)(c). Or the predeceasing spouse may have had a marital property interest in the life insurance policy if the surviving spouse was the insured and the record owner. Wis. Stat. § 766.61(3)(a), (b). Finally, section 766.70(7) appears to apply if a life insurance policy insuring the surviving spouse is owned by a third person and at least one premium was paid from marital property funds after the determination date. Wis. Stat. § 766.61(3)(d).

Section 766.70(7) applies only if all or part of the policy is in the decedent spouse's probate estate. Some life insurance policies contain contractual provisions permitting a nontestamentary transfer of ownership upon the owner's death. If such a contractual provision applies to the predeceasing spouse's interest in the policy, section 766.70(7) will not apply.

Section 766.70(7) applies only to life insurance policies described in section 766.61. Therefore, it does not apply to other types of life

insurance policies—for example, a life insurance policy owned by the decedent spouse insuring a child, a parent, or a business partner.

### **b. Deferred Employment Benefits [§ 12.69]**

It is difficult to imagine when the option to purchase contained in section 766.70(7) would apply to a deferred-employment-benefit plan. Section 766.70(7) applies only if all or part of the plan is included in the decedent spouse's probate estate. Generally, death benefits from deferred-employment-benefit plans are not subject to administration. Wis. Stat. § 853.18(1)(c). Also, if the nonemployee spouse dies first, that spouse's marital property interest in deferred-employment-plan benefits terminates. Wis. Stat. §§ 766.31(3), .62(5).

Therefore, section 766.70(7) seems to apply only if the employee spouse dies first and designates his or her estate as beneficiary of the plan benefits. In the unlikely event of such a designation, the surviving spouse would be able to purchase from the estate the decedent's interest in the plan. *See supra* §§ 2.110, 8.59.

## **J. Elections by Surviving Spouse [§ 12.70]**

### **1. In General [§ 12.71]**

Under section 861.02, the surviving spouse has the right to make the deferred marital property election. *See infra* §§ 12.136–.147. If this election is not made within prescribed time limits, it is lost. *See infra* § 12.139. In certain circumstances, moreover, the decedent's will may put the surviving spouse to an equitable election under section 853.15. *See supra* §§ 12.22–.26. The existence of the spousal elections is another reason why the personal representative may wish to consider advising the surviving spouse to have separate representation. *See supra* § 12.58.

### **2. Disclaimer by Surviving Spouse [§ 12.72]**

Section 854.13(9) provides that a disclaimed interest in survivorship marital property passes to the decedent's probate estate. Section 854.13(7) permits the transferor of the property to specify how the

disclaimed property devolves. It appears that section 854.13(7) conflicts with section 854.13(9). Thus, it may be necessary to commence a probate proceeding, otherwise unnecessary, to receive the decedent's interest in disclaimed survivorship marital property.

## VII. Inventory [§ 12.73]

Section 858.01 requires the personal representative to file an inventory of the decedent's property "within a reasonable time" but no later than six months after appointment unless the court extends or shortens the time. An inventory must be prepared but is not required to be filed for informal administration. Wis. Stat. § 865.11. The inventory required by section 858.01 must show, as of the date of death, the value of all property, what property is marital property, and the type and amount of existing obligations relating to any item of property.

➤ **Comment.** Section 858.07, which governs the contents of the inventory, differs in some respects from section 858.01. First, section 858.01 requires the personal representative to file an inventory of "all property owned by the decedent." Section 858.07 requires the personal representative to include in the inventory "all property subject to administration." Second, section 858.01 requires the personal representative to show "the type and amount of any existing obligation relating to any item of property." Section 858.07 requires the personal representative to include in the inventory "a statement of any encumbrance, lien or other charge upon each item." Presumably, the phrase, "all property owned by the decedent" in section 858.01 means property subject to administration. Likewise, the types of obligations required to be listed by section 858.01 are the same as the obligations required to be listed by section 858.07.

➤ **Practice Tip.** As noted above, section 858.01 requires the personal representative to show on the inventory what property is marital property. For purposes of the inventory, the personal representative should simply list the decedent's interest in marital or nonmarital property, whether it is a fractional interest or an entire interest. It is not necessary to distinguish between individual property and predetermination date property, nor is it necessary to subdivide predetermination date property into deferred marital property and nondeferred marital property. The surviving spouse has no elective rights with respect to deferred marital property. The surviving spouse

has the right to elect an amount, not an interest in property. *See infra* §§ 12.136–.147.

Showing marital property assets on the inventory is substantially the same as showing tenancy-in-common assets. In both cases, the decedent spouse had a fractional ownership interest in the asset. If the entire asset was marital property, the decedent's interest in the asset is one-half. If the asset was mixed property, the decedent's interest will be one-half of the former marital property component plus any other interest the decedent may have had in the asset. Listing marital property assets on the inventory is illustrated by the following example:

<b>Property Subject to Administration</b>	<b>Value of Decedent's Interest at Date of Death</b>
200 shares of XYZ stock, value of \$130 per share, 30% marital property, 70% solely owned by decedent.	
15% marital property interest = \$ 19.50	
70% nonmarital property interest = \$ <u>91.00</u>	
85% interest = \$110.50	
<b>200 shares × \$110.50 =</b>	<b>\$ 22,100</b>

## **VIII. Accounts [§ 12.74]**

### **A. In General [§ 12.75]**

Section 862.05 requires an accounting by the personal representative of the decedent's property and all profits and income from the estate:

Every personal representative shall be charged in the personal representative's accounts with all the property of the decedent which comes to the personal representative's possession; with all profit and income which comes to the personal representative's possession from the estate and with the proceeds of all property of the estate sold by the personal representative.

## **B. Property Owned by Surviving Spouse and in Possession of Personal Representative [§ 12.76]**

Under the Act, the personal representative may possess property in which the surviving spouse has an ownership interest. For example, if an entire asset is marital property, the personal representative and the surviving spouse are tenants in common as to an undivided one-half interest each. The personal representative and the surviving spouse should discuss how the asset will be managed during administration. If the asset was held solely by the decedent, the personal representative manages the entire asset, absent an order of the probate court, until other arrangements are made. However, only one-half of the asset is subject to administration, and the personal representative's accounts must reflect that fact. If the personal representative is receiving and disbursing all items of income and expense regarding the asset, the personal representative may conclude that an account reflecting the surviving spouse's interest in the net income of the property is necessary. This provides a record for the personal representative. However, this *suspense account* should not be part of the probate accounting. It is a separate account and not subject to administration.

➤ **Practice Tip.** If the personal representative is administering the entire asset, including the surviving spouse's one-half interest, the personal representative may request a management fee from the surviving spouse. Section 857.04(2) provides that to the extent possible, the personal representative is to pay special expenses attributable to management and control of marital property from the marital property generating the expenses. *See supra* § 12.55. This section does not authorize the personal representative to charge a management fee, but that certainly would be a reasonable request in most circumstances. Section 857.04(2) appears to apply to the situation in which the personal representative is managing both halves of the marital property.

## **C. Property Owned by Personal Representative and in Possession of Surviving Spouse [§ 12.77]**

There will be situations in which the decedent spouse had a marital property interest in property titled or held solely in the surviving spouse's name. The decedent's marital property interest is subject to

administration. The decedent's interest is shown on the inventory, and items of income and expense attributable to that interest are reflected on the final account. Wis. Stat. § 862.05. The personal representative will need to work with the surviving spouse to determine how the decedent's interest will be managed during administration. The asset may be retitled in accordance with its classification. Wis. Stat. § 857.01. The personal representative may choose to permit the surviving spouse to manage the decedent's interest, receive the income, and pay expenses. In this case, the surviving spouse may ask the estate to pay a management fee. However, the personal representative's fractional interest in such income and expenses must be reflected on the final account.

#### **D. Net Probate Income Attributable to Elected Deferred Marital Property Amount [§ 12.78]**

In addition to accounting for the decedent's fractional interest in an asset's income, the personal representative must determine any net probate income payable to the surviving spouse if the deferred marital property election is made.

The question arises whether section 701.20 applies to net probate income attributable to the elected deferred marital property amount. Section 701.20(5)(d) provides that a legatee of a specific amount of money not determined by pecuniary formula may not be paid any part of the income of the estate but must receive interest on any unpaid amounts at the legal rate set forth in section 138.04 for the period commencing one year after the decedent's death. Section 701.20(5)(b)2. provides that net probate income must be distributed proportionately to all other legatees and devisees.

A surviving spouse who has elected the deferred marital property amount is not a legatee or devisee. Thus, the distribution of net probate income attributable to the elected deferred marital property appears not to be covered by section 701.20. Rather, it appears that the electing spouse is treated as a general creditor with respect to the deferred marital property amount and is not entitled to any net probate income.

## **IX. Tax Accounting During Administration [§ 12.79]**

In addition to preparing an account for purposes of the probate proceeding, the personal representative must file necessary federal and Wisconsin fiduciary income tax returns. *See supra* ch. 9. One-half the income attributable to marital property is taxable to the decedent's estate and the other half is taxable to the surviving spouse. *United States v. Merrill*, 211 F.2d 297 (9th Cir. 1954); *Bishop v. Commissioner*, 152 F.2d 389 (9th Cir. 1945).

## **X. Satisfaction of Obligations After Death of Spouse [§ 12.80]**

### **A. In General [§ 12.81]**

Sections 12.82–.131, *infra*, discuss satisfaction of obligations after the death of a spouse. The subject is extraordinarily complicated. For purposes of discussion, it is assumed that one spouse (either the decedent or the survivor) is obligated and one spouse is not obligated. If both spouses are obligated, much of the discussion is immaterial. For an extensive discussion of obligations generally, see chapters 5 and 6, *supra*.

Section 766.55(2) applies to the satisfaction of obligations during the marriage. That section creates six categories of obligations:

1. Duty of support, Wis. Stat. § 766.55(2)(a);
2. Family-purpose obligation, Wis. Stat. § 766.55(2)(b);
3. Premarital obligation, Wis. Stat. § 766.55(2)(c)1.;
4. Pre-Act obligation, Wis. Stat. § 766.55(2)(c)2.;
5. Tort obligation, Wis. Stat. § 766.55(2)(cm); and
6. Other obligation, Wis. Stat. § 766.55(2)(d).

*See also supra* § 5.32.



➤ **Comment.** The availability of marital property to satisfy family-purpose obligations is one of the very significant concepts in the Marital Property Act. *See supra* chs. 5, 6. This provision has a significant effect on the allowance and satisfaction of claims at the death of a spouse.

Section 766.55(8) provides that after the death of a spouse, property is available for satisfaction of obligations as provided in section 859.18. If a claim filed against the decedent's estate is one for which property is available under section 859.18, the claim must describe which of the six types of obligations under section 766.55(2) applies to the claim. Wis. Stat. § 859.13.

➤ **Note.** The Legislative Council notes on section 859.18 include a chart outlining property available for satisfaction of obligations at the death of a spouse. *See* Wis. Stat. Ann. § 859.18 Legis. Council Notes—1985 Act 37, § 169 (West 2002).

➤ **Note.** Section 701.065 sets forth a claims procedure that limits the time within which creditors can recover from trustees who have a duty or power to pay a decedent's debts. While the claims procedure in chapter 701 does not contain a reference to the extensive marital property provisions and exemptions contained in chapter 859 of the Probate Code, it appears that the provisions of section 859.18 apply to property held by a trustee at the time of death. Notwithstanding its location in the Probate Code, section 859.18 is not limited to assets subject to administration.

If the trust was irrevocable before the date of the decedent's death, the trust normally would not contain marital property because a completed gift would have been made. *See supra* § 2.102 (irrevocable trusts). However, if the trust was revocable, the trust could contain former marital property.

## **B. Effect of Marital Property Agreements [§ 12.82]**

Section 859.18(6) provides that a marital property agreement as defined under section 766.01(12) does not affect property available for satisfaction of obligations under section 859.18. Section 766.01(12)

defines a marital property agreement as an agreement that complies with sections 766.58, 766.585, 766.587, 766.588, and 766.589.

According to section 766.55(4m), no provision of a marital property agreement or a decree under section 766.70 adversely affects the interest of a creditor unless the creditor had actual knowledge of that provision when the obligation to that creditor was incurred, or in the case of an open-end plan as defined in section 766.555(1)(a), when the plan was entered into.

It appears that section 859.18(6) is designed to apply when a marital property agreement is used to effect a nontestamentary disposition pursuant to section 766.58(3)(f) (the “Washington will” provision). As previously noted, section 859.18(6) states that a marital property agreement may not affect property that is available for satisfaction of obligations under section 859.18. Section 859.18(2) provides that property that would have been available to the creditor under section 766.55(2) continues to be available after the death of a spouse. Therefore, if the creditor had actual knowledge of a marital property agreement, marital property reclassified by the agreement is not available under section 859.18. Wis. Stat. § 766.55(4m). If the creditor did not have actual knowledge of an agreement, the property is available under section 859.18. *Id.* Thus, it appears that section 859.18(6) is designed to apply to nontestamentary dispositions under marital property agreements pursuant to section 766.58(3)(f). The reason for this is set forth in the Legislative Council notes on section 859.18:

In deciding what property should be available to satisfy an obligation at the death of a spouse, the special committee first looked to whether the property is available under current law. Thus, joint tenancy, deferred employment benefits and insurance were made exceptions to the general rule of availability and certain trusts and accounts are available subject to the limitations under existing law. The special committee also recommended that survivorship marital property not be generally available because survivorship marital property is similar to joint tenancy .... To balance the latter exclusion [survivorship marital property] from the pool of property available to creditors, the special committee concluded that a marital property agreement [under section 766.58(3)(f)] should not be able to affect the property available for satisfaction of an obligation at the death of a spouse. In practice, the latter rule may not be as significant as it initially appears because if [nontestamentary dispositive provisions of] marital property agreements could affect property available to satisfy obligations at the death of a spouse, a creditor would only be bound by agreement if the

creditor had actual knowledge of the relevant term of the agreement [i.e. the nontestamentary dispositive provision]; if the creditor has actual knowledge, it is likely that the amount of credit extended would be reduced.

Wis. Stat. Ann. § 859.18 Legis. Council Notes—1985 Act 37, § 169 (West 2002).

In sum, if the creditor relies on the availability of marital property assets in extending credit and the marital property assets subsequently become joint tenancy property or survivorship marital property, the property is not available to the creditor after the spouse's death. This was the case before the Act. On the other hand, if the creditor relies on the availability of marital property assets in extending credit and the property is transferred at death by will or by marital property agreement, the marital property assets remain available to the creditor.

### **C. Wisconsin Tax Obligations [§ 12.83]**

Section 71.91(3) provides that all tax obligations to Wisconsin, including interest, penalties, and costs incurred during marriage by a spouse after December 31, 1985, or after both spouses are domiciled in Wisconsin, whichever is later, are incurred in the interest of the marriage or family and may be satisfied only under sections 766.55(2)(b) and 859.18. However, section 71.91(3) also provides that if one spouse is relieved of liability under section 71.10(6)(a), (b), or (6m), the other spouse's tax obligation to Wisconsin may be satisfied only under section 766.55(2)(d) or by set-off under section 71.55(1), 71.61(1), or 71.80(3) or (3m). *See supra* ch. 9 (when spouse relieved of liability).

Thus, for the most part, Wisconsin tax obligations are family-purpose obligations. When a family-purpose obligation is discussed in this chapter, it may include a Wisconsin tax obligation.

Section 859.18(3) contains a special rule that applies when credit is granted by a person who regularly extends credit. That rule is discussed in section 12.90, *infra*. It should be noted, however, that the special rule in section 859.18(3) is expressly made applicable to Wisconsin tax obligations as well.

➤ **Note.** The Act does not contain specific provisions applicable to United States tax obligations or county or municipal obligations. *See supra* § 6.19.

## **D. Obligations of Spouses Under Section 766.55(2)** **[§ 12.84]**

### **1. Support Obligations and Family-purpose Obligations [§ 12.85]**

#### **a. In General [§ 12.86]**

Section 766.55(2)(a) provides that after the determination date, a spouse's obligation to satisfy a duty of support owed to the other spouse or to a child of the marriage may be satisfied only from all marital property and all other property of the obligated spouse. *See supra* ch. 5, 6.

Section 766.55(2)(b) provides that after the determination date, an obligation incurred by the spouse in the interest of the marriage or the family may be satisfied only from all marital property and all other property of the incurring spouse. *See supra* chs. 5, 6.

Sections 12.87–.94, *infra*, discuss the satisfaction of support and family-purpose obligations after one spouse dies.

#### **b. Obligated Spouse Dies First [§ 12.87]**

##### **(1) Obligated Spouse's Probate Property** **[§ 12.88]**

Under the common law property system, if the obligated spouse died first, creditors could file a claim in the estate under section 859.01. All assets in the probate estate were available for payment of the claim. The result under the marital property system is the same and for the same reason: the decedent spouse was personally liable.

## (2) Obligated Spouse's Nonprobate Transfers [§ 12.89]

If the obligated spouse dies first and has transferred assets by nonprobate means, some of those assets are exempt from creditors' claims under section 859.18(4)(a). The exempt property is

1. Survivorship marital property, except for certain encumbrances specified in section 766.60(5)(b) and (c);
2. Joint tenancy property in which the decedent spouse was a tenant, subject to any judgment lien on which execution was issued before death;
3. Deferred employment benefits arising from the decedent's employment; and
4. Proceeds of a life insurance policy insuring the decedent if the proceeds are not payable to the decedent's estate and are neither assigned to the creditor as security nor payable to the creditor.

➤ **Note.** Notice that section 859.18(4)(a)4. applies if life insurance proceeds are paid to the decedent's estate, but that section 859.18(4)(a)3., which applies to deferred employment benefits, is not so limited.

Section 859.18(5) states that if certain specified assets transferred by nonprobate means are otherwise available under section 859.18, they remain available. The list is not exclusive. The assets are

1. Trusts described in section 701.07(3) (funded revocable trusts);
2. Spendthrift trusts described in section 701.06; and
3. Accounts in financial institutions governed by chapter 705 and described in section 705.07.

Under section 859.18(2), when one spouse dies, property that would have been available to the creditor if the marriage had continued remains available except as provided in subsections 859.18(3)–(5). Section

859.18(2) specifically provides for tracing if the property is sold or exchanged.

➤ **Comment.** The extent to which section 859.18(2) applies to nonprobate transfers is unclear. Under Wisconsin's common law property system before 1986, assets transferred by nonprobate means were not available to a creditor unless made available by a specific statute. Section 859.18(2) may enlarge creditor's rights with respect to nonprobate assets.

### **(3) Surviving Nonobligated Spouse's Property [§ 12.90]**

Under the pre-Act common law property system, assets of the surviving nonobligated spouse were not available to a creditor because collection depended on personal liability. The result under the marital property system is quite different. Under section 859.18(2), if the obligated spouse dies first, the surviving spouse's property that would have been available to the creditor had the marriage continued remains available to the creditor. Section 859.18(2) specifically provides for tracing in the event of a subsequent sale or exchange. Unless the obligation resulted either from an extension of credit by a person who regularly extends credit or from a tax obligation to the state of Wisconsin, the surviving spouse's income is not available, and the surviving spouse's interest in former marital property is available only to the extent of the value of the marital property at the decedent's death. Wis. Stat. § 859.18(3). However, if the obligation resulted from an extension of credit by a person who regularly extends credit or if the obligation was a Wisconsin tax obligation, the surviving spouse's income is available, and the surviving spouse's interest in former marital property is not limited to the value of the marital property at the decedent's death. In effect, the marital property regime continues for the surviving spouse with respect to certain creditors. *Park Bank-West v. Mueller*, 151 Wis. 2d 476, 444 N.W.2d 754 (Ct. App. 1989).

**c. Nonobligated Spouse Dies First [§ 12.91]****(1) Nonobligated Spouse's Probate Property  
[§ 12.92]**

Under the pre-Act common law property system, if the nonobligated spouse died first, the creditor did not file a claim in the estate of the nonobligated spouse. Collection depended on personal liability. The marital property system differs considerably. Under section 859.18(2), when a spouse dies, property that was available to the creditor during the marriage continues to be available. That section specifically provides for tracing in the event of a sale or exchange. Therefore, if the nonobligated spouse's probate estate contains former marital property assets and those assets were available to the creditor during the marriage, the assets continue to be available after the nonobligated spouse's death. The creditor must file a timely claim under section 859.01 to preserve the creditor's rights against the property.

If the obligation is not in default, the creditor may not be able to accelerate the obligation by filing a claim. However, if the claim is not filed in a timely manner as a contingent claim, it is barred against the estate in the event of a subsequent default.

**(2) Nonobligated Spouse's Nonprobate  
Transfers [§ 12.93]**

If the nonobligated spouse dies first and has transferred assets by nonprobate means, some of those assets may be available to the creditor, and some may not be. Section 859.18(4)(b) states that transfers of certain nonprobate assets to a third person are exempt. These assets are

1. The decedent's interest in joint tenancy property, subject to any judgment lien on which execution was issued before death;
2. Deferred employment benefits arising from the decedent's employment; and
3. The proceeds of a life insurance policy insuring the decedent's life if the proceeds are not payable to the decedent's estate and are neither assigned to the creditor as security nor payable to the creditor.

➤ **Note.** Notice that section 859.18(4)(b)3. applies if life insurance proceeds are paid to the decedent's estate, but that section 859.18(4)(b)2., which applies to deferred employment benefits, is not so limited.

Under the pre-Act common law property system, collection depended on personal liability, and unsecured creditors were not able to reach nonprobate assets in the hands of the recipients unless those assets were made specifically available by statute. Under section 859.18(5), certain nonprobate assets, if otherwise available under section 859.18, remain available under other statutes. These assets are

1. Trusts described in section 701.07(3) (funded revocable trusts);
2. Spendthrift trusts described in section 701.06; and
3. Accounts in financial institutions governed by chapter 705 and described in section 705.07.

➤ **Note.** Section 701.065 sets forth a claims procedure that limits the time in which creditors can recover from trustees who have a duty or power to pay a decedent's debts.

Under section 859.18(2), when one spouse dies, property that would have been available to the creditor if the marriage had continued remains available except as provided in subsections 859.18(3)–(5). Section 859.18(2) specifically provides for tracing if the property is sold or exchanged.

➤ **Comment.** The extent to which section 859.18(2) applies to nonprobate transfers is unclear. Under Wisconsin's common law property system before 1986, assets transferred by nonprobate means were not available to a creditor unless made available by a specific statute. Section 859.18(2) may enlarge creditor's rights with respect to nonprobate assets.



### **(3) Surviving Obligated Spouse's Property** **[§ 12.94]**

Under the common law property system, if the nonobligated spouse died first, all the assets owned by the surviving spouse were available because the surviving spouse was personally liable. The same result generally obtains under the marital property system, for the same reason: the obligated spouse is personally liable.

➤ *Query.* What if assets in the nonobligated spouse's probate estate were available to the creditor, the creditor did not file a claim on a timely basis under section 859.01, and those assets are distributed to the surviving obligated spouse? Section 859.02(1) provides that claims not filed on a timely basis are forever barred against the estate, the personal representative, and the decedent's heirs and beneficiaries. However, section 859.02(3) provides that the failure to file a timely claim against a decedent's estate does not bar the claimant from satisfying the claim from property other than the decedent's estate. Since the surviving spouse is personally liable, assets that are immune from claims of creditors in the probate estate seem to lose their immunity if distributed to the surviving spouse. However, if such immune assets are distributed to someone other than the surviving spouse, the immunity continues.

## **2. Premarriage Obligations and Pre-Act Obligations** **[§ 12.95]**

### **a. In General [§ 12.96]**

Section 766.55(2)(c) provides that

1. An obligation incurred by a spouse before or during marriage that is attributable to an obligation arising before marriage or to an act or omission occurring before marriage may be satisfied only from property of that spouse that is not marital property and from that part of marital property which would have been the property of that spouse but for the marriage.

2. An obligation incurred by a spouse before, on or after January 1, 1986, that is attributable to an obligation arising before January 1, 1986, or to an act or omission occurring before January 1, 1986, may be satisfied only from property of that spouse that is not marital property and from that part of

marital property which would have been the property of that spouse but for the enactment of this chapter.

Section 766.55(2)(c) introduces a new concept in Wisconsin. *See supra* §§ 5.32, ch. 6. Under the common law property system, a creditor's collection rights depended on personal liability. *See supra* § 5.3. Once a judgment establishing personal liability was entered, the creditor could use the collection process to reach the debtor's property. The Marital Property Act modifies that concept as it applies to premarital and pre-Act obligations.

Under section 766.55(2)(c), some property may be available for an obligation, and other property may not. The personal representative must keep this in mind while administering the estate. It may be necessary to segregate certain assets.

The purpose of section 766.55(2)(c) is to prevent a windfall to the creditor merely by virtue of the marriage or the application of the Act. Conversely, the purpose of that section is also to prevent the creditor from being adversely affected by the marriage or application of the Act. Therefore, the usual collection rules based on the availability of marital property and personal liability do not apply. Under section 766.55(2)(c), a creditor may not be able to reach all property owned by the debtor spouse even though that spouse is personally liable.

➤ **Example.** Assume that a debtor spouse owns a marital property interest in the other spouse's wages. Even though the debtor owns part of the other spouse's wages, those wages are not available to the creditor if the obligation is a premarital obligation or predetermination date obligation.

➤ **Note.** The chart in the Legislative Council notes on section 859.18 does not appear to take section 766.55(2)(c) into account. *See* Wis. Stat. Ann. § 859.18 Legis. Council Notes—1985 Act 37, § 169 (West 2002). There is a statement in the notes to the effect that the chart is only a general outline. Section 766.55(2)(c) is one instance in which the chart is not technically accurate.

➤ **Comment.** Section 766.55(2)(c) is a "straddle provision" that will diminish in significance as Wisconsin moves away from the Act's effective date. However, there will always be some "straddle

obligations” because the obligation was incurred either before the effective date of the Act or before the decedent’s determination date, which may be after January 1, 1986.

## **b. Obligated Spouse Dies First [§ 12.97]**

### **(1) Obligated Spouse’s Probate Property [§ 12.98]**

Under the pre-Act common law property system, if the obligated spouse died first, the assets in the probate estate were available to the creditor if a timely claim was filed. That is not true under Wisconsin’s marital property system. All the assets in the probate estate are available (assuming a timely claim was filed under section 859.01) unless the obligation is a premarriage or pre-Act obligation. In that event, if the probate estate contains any property that would not have been the decedent’s but for the marriage or the enactment of the Act, it is not available. *See* Wis. Stat. § 766.55(2)(c). For example, if the decedent’s estate contains any former marital property derived solely from the surviving spouse’s wages, that property is not available to the creditor, even though the decedent was personally liable to the creditor.

### **(2) Obligated Spouse’s Nonprobate Transfers [§ 12.99]**

If the obligated spouse dies first and has transferred assets by nonprobate means, some of those assets are specifically exempt from creditors’ claims, and some are not. *See supra* § 12.89.

➤ **Note.** Apparently, the straddle provisions of section 766.55(2)(c) do not apply to nonprobate assets. Section 859.18(2) incorporates the straddle provisions of section 766.55(2)(c), but subsections 859.18(4) and (5), which apply to nonprobate transfers, are an express exception to section 859.18(2).

### **(3) Surviving Nonobligated Spouse's Property [§ 12.100]**

Generally, if the obligated spouse dies first and the obligation is a predetermination date obligation, the surviving spouse's assets are not available to the creditor. However, section 766.55(2)(c) has a special rule for these obligations. Property owned by the surviving spouse that would have been the property of the obligated spouse but for the marriage or but for the Act is available to the creditor. Wis. Stat. §§ 859.18(2), 766.55(2)(c). The chart that is part of the Legislative Council notes on section 859.18 does not reflect this fact. *See* Wis. Stat. Ann. § 859.18 Legis. Council Notes—1985 Act 37, § 169 (West 2002).

➤ *Example.* At the time of his death, a husband held a savings account in his sole name. The account contained marital property solely derived from his wages. The wages were deposited in the account after the determination date and, thus, were marital property. One-half of the account is included in the decedent's probate estate. The other half of the account, which belongs to the surviving spouse, is available to the decedent's pre-Act creditor even though the surviving spouse is not obligated to the creditor.

#### **c. Nonobligated Spouse Dies First [§ 12.101]**

##### **(1) Nonobligated Spouse's Probate Property [§ 12.102]**

Under the common law property system, when the nonobligated spouse died first, creditors did not file a claim in the estate because collection depended on personal liability. However, under the marital property system, some of the nonobligated spouse's interests in probate assets may be available. Therefore, creditors can file claims under section 859.01. Under section 766.55(2)(c), when there is a predetermination date obligation and the nonobligated spouse dies first, the nonobligated spouse's interest in former marital property that would have been the property of the obligated spouse but for the marriage or but for the Act remains available. Wis. Stat. § 859.18(2).

➤ **Example.** Assume that a surviving obligated spouse's wages were used to purchase an asset in the decedent's probate estate that was marital property. The decedent's former marital property interest in the asset is available.

## **(2) Nonobligated Spouse's Nonprobate Transfers [§ 12.103]**

If the nonobligated spouse dies first and has transferred certain assets by nonprobate means to a third person, some assets are specifically exempt from the claims of creditors, and some may not be. Wis. Stat. § 859.18(4)(b); *see supra* § 12.93.

## **(3) Surviving Obligated Spouse's Property [§ 12.104]**

Generally, if the surviving spouse is the obligated spouse, all assets owned by the obligated spouse are available to the creditor. However, because of the special rule in section 766.55(2)(c), *see supra* § 12.100, which is made applicable by section 859.18(2), some assets owned by the surviving spouse may not be available to the creditor. These are assets that would not have belonged to the surviving spouse had there been no marriage or no Act.

➤ **Example.** Assume that the wages of a nonobligated now-deceased spouse were used to purchase an asset that is marital property. Even though the surviving obligated spouse owns a one-half interest in the former marital property, it is not available to the creditor.

If a creditor has a claim against the estate of the deceased nonobligated spouse but fails to file the claim, the claim is barred against the estate. However, if assets in the estate are distributed to the surviving obligated spouse, it appears that the assets are no longer barred from the creditor's claim. *See supra* § 12.94.

### 3. Torts [§ 12.105]

#### a. In General [§ 12.106]

Section 766.55(2)(cm) provides as follows: “An obligation incurred by a spouse during marriage, resulting from a tort committed by the spouse during marriage, may be satisfied from the property of that spouse that is not marital property and from that spouse’s interest in marital property.”

It is not clear whether section 766.55(2)(cm) applies to all torts or only to family-purpose torts (i.e., torts committed in the interest of the marriage or the family). Read literally, section 766.55(2)(cm) applies to all torts. However, if it does, why does section 766.55(2)(d) refer to “acts or omissions”? *See infra* §§ 12.115–.123 (discussing obligations under section 766.55(2)(d)). One construction is that section 766.55(2)(cm) applies to family-purpose torts and section 766.55(2)(d) applies to other torts. Another interpretation is that section 766.55(2)(cm) applies to all torts and section 766.55(2)(d) applies to acts or omissions that are not torts (e.g., contractual liabilities and civil and criminal forfeitures). This book adopts the latter construction. *See supra* §§ 5.32, 6.26–.28.

➤ **Note.** Different results may occur depending on the correct construction of section 766.55(2)(cm). Section 766.55(2)(d) has an order of satisfaction, whereas section 766.55(2)(cm) does not. *See infra* § 12.115.

Another ambiguity exists with respect to torts committed during the marriage and before the determination date. Section 766.55(2)(cm) does not distinguish between torts committed before and after the determination date. It applies to all torts committed by a spouse “during marriage.” On the other hand, section 766.55(2)(c)2. applies to obligations incurred by a spouse before, on or after January 1, 1986. For a discussion of this ambiguity, see section 5.32, *supra*.

➤ **Note on Terminology.** This chapter refers to torts committed during marriage before January 1, 1986, as *straddle torts*.

**b. Obligated Spouse Dies First [§ 12.107]****(1) Obligated Spouse's Probate Property  
[§ 12.108]**

If section 766.55(2)(cm) applies and the spouse who committed the tort dies first, all of that spouse's probate assets are available to the injured person on the theory of personal liability. This includes the decedent's interest in former marital property. However, if the tort is a straddle tort, *see supra* § 12.106, so that section 766.55(2)(c)2. applies, then the obligation is satisfied in the same manner that a predetermination date obligation is satisfied. *See supra* §§ 12.97–.100.

**(2) Obligated Spouse's Nonprobate Transfers  
[§ 12.109]**

If the tortfeasor spouse dies first and transfers both halves of items of marital property by nonprobate means, some of the items transferred by nonprobate means are available, and some are not. *See supra* § 12.89. Again, the result may differ depending on whether section 766.55(2)(c)2. or section 766.55(2)(cm) applies. *See supra* § 12.106.

**(3) Surviving Nonobligated Spouse's  
Property [§ 12.110]**

If section 766.55(2)(cm) applies and the tortfeasor spouse dies first, none of the surviving spouse's property is available to the injured person. Section 859.18(2) provides that property that would have been available under section 766.55(2) during the marriage remains available. If section 766.55(2)(cm) applies, the nonobligated spouse's marital property interest is not available under section 766.55(2). However, if section 766.55(2)(c)2. applies, the tort obligation may be satisfied in the same manner as a predetermination date obligation, and certain property of the surviving spouse may be available. *See supra* §§ 12.97–.100.

**c. Nonobligated Spouse Dies First [§ 12.111]****(1) Nonobligated Spouse's Probate Property  
[§ 12.112]**

If section 766.55(2)(cm) applies and the nonobligated spouse predeceases the tortfeasor spouse, none of the assets in the estate are available. Wis. Stat. §§ 766.55(2)(cm), 859.18(2). However, if section 766.55(2)(c)2. applies, then the tort obligation may be satisfied in the same fashion as a predetermination date obligation is satisfied, and certain assets in the probate estate may be available. *See supra* §§ 12.101–.104.

**(2) Nonobligated Spouse's Nonprobate  
Transfers [§ 12.113]**

If the nonobligated spouse dies first and transfers both halves of items of marital property by nonprobate means, certain of the assets so transferred to a third person are specifically exempt from creditors' claims. Wis. Stat. § 859.18(4)(b); *see supra* § 12.103.

**(3) Surviving Obligated Spouse's Property  
[§ 12.114]**

If section 766.55(2)(cm) applies, all the surviving tortfeasor spouse's assets are available because the surviving spouse is obligated. However, if section 766.55(2)(c)2. applies, then the tort is satisfied just as a predetermination date obligation is satisfied, and certain property of the surviving tortfeasor may not be available. *See supra* §§ 12.101–.104.

**4. Other Obligations [§ 12.115]**

Section 766.55(2)(d) provides that after the determination date “[a]ny other obligation incurred by a spouse during marriage, including one attributable to an act or omission during marriage, may be satisfied only from property of that spouse that is not marital property and from that spouse's interest in marital property, in that order.”



➤ **Comment.** It appears that section 766.55(2)(d) does not apply to torts. *See supra* § 12.106. The distinction is important because section 766.55(2)(d) has a requirement that obligations be satisfied in a prescribed order, whereas section 766.55(2)(cm) does not.

Except for the order-of-satisfaction requirement, creditors' rights under section 766.55(2)(d) closely approximate creditors' rights under the pre-Act common law property system: collection depends on establishing personal liability. *See supra* §§ 5.32, 6.29.

#### **a. Obligated Spouse Dies First [§ 12.116]**

##### **(1) Obligated Spouse's Probate Property [§ 12.117]**

If the obligated spouse dies first, all of that spouse's probate assets are available if a timely claim is filed under section 859.01. However, it appears that the obligation must be satisfied first from nonmarital property, then from the decedent's interest in marital property. *See* Wis. Stat. § 766.55(2)(d); *see also supra* § 12.115.

##### **(2) Obligated Spouse's Nonprobate Transfers [§ 12.118]**

If the obligated spouse dies first, some nonprobate assets are available to the creditor, and some are not. *See supra* § 12.89.

##### **(3) Surviving Nonobligated Spouse's Property [§ 12.119]**

If the surviving spouse is not obligated, none of the surviving spouse's property is available to the creditor.

**b. Nonobligated Spouse Dies First [§ 12.120]****(1) Nonobligated Spouse's Probate Property  
[§ 12.121]**

If the nonobligated spouse dies first and the obligation is an “other” obligation under section 766.55(2)(d), none of the assets in the probate estate are available.

**(2) Nonobligated Spouse's Nonprobate  
Transfers [§ 12.122]**

If the nonobligated spouse dies first, the obligation is an “other” obligation under section 766.55(2)(d), and the predeceasing spouse effects transfers of property by nonprobate means, nonprobate transfers of the decedent's nonmarital property and the decedent's interest in marital property are not available to creditors. However, a nonprobate transfer of the surviving obligated spouse's interest in marital property may be available. *See supra* § 12.93.

**(3) Surviving Obligated Spouse's Property  
[§ 12.123]**

If the nonobligated spouse dies first and the surviving spouse is obligated, all the surviving spouse's property is available to satisfy an “other” obligation under section 766.55(2)(d).

➤ **Comment.** It is not clear whether the order of satisfaction contained in section 766.55(2)(d) must be followed. Administration can be viewed as a continuation or winding up of the marriage. However, once the administration has terminated and the assets are in the surviving spouse's hands, the property of the marriage has clearly been distributed. Once the administration has terminated, it would appear that the order prescribed by section 766.55(2)(d) need not be followed because the marriage has terminated, the property in the surviving spouse's hands is no longer marital property, and the surviving spouse is personally liable.

## **E. Claims [§ 12.124]**

### **1. Filing a Claim [§ 12.125]**

Under section 859.02(1), claims against a decedent's estate, including claims of Wisconsin and any subdivision of Wisconsin, are forever barred against the estate, the personal representative, and the decedent's heirs and beneficiaries unless the claims are filed with the court within the time for filing claims. Under section 859.01, when an application for administration is filed, the court or the probate registrar is required to fix by order the time within which claims are to be filed. The time is three to four months from the date of the order. Wis. Stat. § 859.01.

Section 859.01 does not apply to claims based on

1. Tort;
2. A marital property agreement subject to time limitations under section 766.58(13)(b) or (c);
3. Wisconsin income, franchise, sales, withholding, gift, or death taxes;
4. Unemployment insurance contributions due or benefits overpaid;
5. A claim for funeral or administrative expenses;
6. A state claim under section 46.27(7g), 49.496, or 49.682;
7. A claim of the United States; or
8. A claim involving an action that is pending against the decedent at the time of death and the action survives.

Wis. Stat. §§ 859.02(2)(a), .03.

Under section 701.065, a trustee who has a duty or power to pay the debts of a decedent may commence a claims procedure similar to the claims procedure for estates described above.

## 2. Effect of Failure to File a Claim [§ 12.126]

### a. Obligated Spouse Dies First [§ 12.127]

Assume that the obligated spouse incurred a family-purpose obligation, that the credit was extended by a person who regularly extends credit, and that the obligated spouse dies first. Under section 859.18(2), all property that would have been available to the creditor during the marriage is available after death. However, even if the creditor fails to file a claim in the decedent's estate, the surviving spouse's interest in former marital property is still available to the creditor. Section 859.02(3) provides as follows: "Failure of a claimant timely to file a claim against a decedent's estate does not bar the claimant from satisfying the claim from property other than the decedent's estate."

➤ *Query.* What if assets in the estate against which claims are barred are transferred to the surviving spouse? It appears those assets lose their exemption. Furthermore, the surviving spouse's marital property that was not subject to probate administration remains available.

### b. Nonobligated Spouse Dies First [§ 12.128]

Assume that a family-purpose obligation exists and that the nonobligated spouse dies first. What is the effect of section 859.02(3) if the creditor fails to file a claim in the estate? Since the surviving spouse is obligated, all assets owned by that spouse are available to the creditor. However, because the creditor failed to file a claim in the estate, estate assets otherwise available become exempt, and this exemption continues if the assets are not transferred to the surviving spouse. However, if the assets are transferred to the surviving spouse, the assets seem to lose their exemption as a result of the surviving spouse's personal liability.

## **F. Contribution [§ 12.129]**

### **1. In General [§ 12.130]**

Assume that only one spouse is obligated to a creditor for a family-purpose obligation. The Wisconsin Marital Property Act does not require the creditor to proceed first against property owned by the obligated spouse. Likewise, the Act does not contain any provisions regarding rights of contribution between spouses. *Cf.* Wis. Stat. § 766.70(5). The subject of contribution is beyond the scope of this chapter, and the Act does not deal with the subject. If a right of contribution exists, it is not derived from the Marital Property Act.

### **2. Claims for Reimbursement as a Result of Traceable Mixing [§ 12.131]**

If marital property funds are mixed with nonmarital property assets, mixing occurs. Wis. Stat. § 766.63(1). The court of appeals has held that when mixing is traceable, the surviving spouse has a right of reimbursement, not an ownership interest in the mixed asset. *Kobylski v. Hellstern (In re Estate of Kobylski)*, 178 Wis. 2d 158, 503 N.W.2d 369 (Ct. App. 1993). So, for example, if the decedent owned nonmarital real estate subject to traceable mixing, ownership of the marital property funds has been transferred to the decedent. If the surviving spouse intended a gift to the decedent, the remedies for gift recoveries are available. If the surviving spouse did not intend a gift, the surviving spouse has a claim for reimbursement, which must be filed pursuant to section 859.01.

## **XI. Family Rights [§ 12.132]**

### **A. History of Surviving Spouse's Elective Share [§ 12.133]**

#### **1. Surviving Spouse's Elective One-Third Share Under Common Law Property System [§ 12.134]**

Historically, Wisconsin has protected the surviving spouse against disinheritance by the decedent spouse. Until 1971, the surviving wife had an *inchoate dower right* and the surviving husband had a *curtesy right*. Inchoate dower and curtesy were abolished, effective March 31, 1971, and replaced by a one-third elective share termed *dower* (to be distinguished from inchoate dower). Wis. Stat. §§ 861.03, .05 (1983–84). The elective share consisted of one-third of the net probate estate reduced by any property given outright to the spouse under the decedent's will. Except for property given outright to the spouse under the will (up to such one-third), an election to take the one-third elective share forfeited any other right of the surviving spouse to take under the will and under the laws of intestate succession. Wis. Stat. § 861.05(2) (1983–84).

The one-third elective share was subject to bar by the terms of a written agreement signed by both spouses. Wis. Stat. § 861.07(1) (1983–84). The one-third elective share was also barred if the surviving spouse received at least one-half the total of certain property that generally approximated the adjusted gross estate of the deceased spouse for federal estate tax purposes. Wis. Stat. § 861.07(2) (1983–84).

Wisconsin's one-third elective share did not apply to nonprobate assets.

#### **2. Surviving Spouse's Elections Under Marital Property Act 1986–98 [§ 12.135]**

The Wisconsin Marital Property Act repealed the one-third elective share and replaced it with two new elections: a *deferred marital property election* for assets subject to administration and an *augmented marital property estate election* for nonprobate assets. The rights to

make the deferred marital property election and the augmented marital property estate election became effective on January 1, 1986, and continued for 12 years until December 31, 1998, when they were repealed by 1997 Wisconsin Act 188 and replaced with a single, unified deferred marital property election. *See infra* §§ 12.136–.165.

For an in-depth discussion of the two former elections and their relationship to UMPA's deferred marital property concept, see the second edition of *Marital Property Law in Wisconsin*. Keith A. Christiansen et al., *Marital Property Law in Wisconsin* (2d ed. 1986 & Supp. 1995). The two prior elections are not discussed in this fourth edition of *Marital Property Law in Wisconsin*.

## **B. Deferred Marital Property Election [§ 12.136]**

### **1. In General [§ 12.137]**

1997 Wisconsin Act 188, effective for deaths occurring on or after January 1, 1999, combined the former deferred marital property election in probate assets and the former augmented marital property estate election against nonprobate assets into a single, unified deferred marital property election.

The *Drafting Committee Notes to 1997 Wisconsin Act 188—Revision of Wisconsin Probate Code*, reprinted in Howard S. Erlanger, *Wisconsin's New Probate Code—A Handbook for Practitioners* app. C at 42 (1998), describe the following major changes from Wisconsin's prior deferred marital property election:

1. The election is now based on the amount of all deferred marital property owned by both spouses (the *augmented deferred marital property estate*), not just that owned by the decedent. The surviving spouse is entitled to half that total, rather than half the deferred marital property owned by the decedent.
2. Separate elections for probate and nonprobate deferred marital property have been eliminated and replaced by a single election.
3. The “all or nothing” bar in the prior probate election, *see* Wis. Stat. § 861.13 (1995–96), has been eliminated.

4. The election is for a pecuniary amount, rather than a fractional interest in assets.
5. All nonprobate assets are in the augmented deferred marital property estate regardless of the date of execution of the governing instrument. The April 4, 1984, effective date for the prior augmented marital property estate election has been repealed.
6. The election is made by verified petition rather than election form.

## **2. Who May Make the Election [§ 12.138]**

A surviving spouse is eligible to make a deferred marital property election if at the time of the decedent's death, the decedent was domiciled in Wisconsin. Wis. Stat. § 861.02(7)(a). The decedent's representatives, successor, or assigns may not make a deferred marital property election. An exception applies if the surviving spouse unlawfully and intentionally killed the decedent. In that case, the decedent's estate has the right to elect no more than 50% of the augmented deferred marital property estate. Wis. Stat. § 861.02(8). This provision is intended to reverse *Krueger v. Rodenberg*, 190 Wis. 2d 367, 527 N.W.2d 381 (Ct. App. 1994), in which the court held that a decedent wife's estate had no right to claim any interest in predetermination date property owned by her surviving husband, even though the husband had murdered the wife. The election must be made by the surviving spouse or by the surviving spouse's conservator, guardian, guardian ad litem, or agent under a power of attorney. Wis. Stat. § 861.09. The right of election is personal to the surviving spouse. If the surviving spouse dies before the election is made, the right to elect terminates. *Id.*

## **3. Procedure for Making Election [§ 12.139]**

Section 861.08 sets forth the procedure the surviving spouse must follow to make a deferred marital property election. Unless the time is extended, the surviving spouse must, within six months after the date of the decedent's death, do all the following:

1. File a petition for the deferred marital property election with the probate court or, if no judicial proceeding is pending, with the court



that has jurisdiction of probate proceedings located in the county of the decedent's residence;

➤ **Note.** All petitions to the probate court must be verified. Wis. Stat. § 879.01.

2. Mail or deliver a copy of the petition to the personal representative, if any, of the decedent's estate; and
3. Give notice, in the manner provided in chapter 879, of the time and place set for hearing the petition to any persons who may be adversely affected by the election.

➤ **Comment.** Presumably, persons adversely affected include the transferees of deferred marital property even though the probate court may not have jurisdiction over the transferees.

Wis. Stat. § 861.08.

➤ **Practice Tip.** Note that the surviving spouse, not the personal representative or the court, must give notice of the hearing. The surviving spouse will most likely need assistance with the mailing of the notice as well as with the preparation of the verified petition.

The court may grant the surviving spouse an extension of time for making the election with cause shown. Wis. Stat. § 861.08(3)(a). The petition for extension of time must be filed within six months of the decedent's death unless (1) the surviving spouse was prevented from filing the petition for reasons beyond the spouse's control, and (2) failure to extend the time would result in hardship. Wis. Stat. § 861.08(3)(b).

➤ **Note.** Since the election is made by petition filed with the court, it is not possible to make the election in informal administration.

The surviving spouse may not be aware of the existence of the deferred marital property election or may not have the information necessary to calculate the election amount. There is no statutory duty, however, on the part of the personal representative to advise the surviving spouse about the existence of the election or to assist the spouse with the calculations. See *Schadde v. Estate of Schadde*, No. 90-0542-FT, 1991 WL 97310 (Wis. Ct. App. Apr. 25, 1991) (unpublished).

opinion not citable per section 809.23(3)) (holding that personal representative does not have duty to inform surviving spouse of six-month deadline for filing deferred marital property election, citing *Ludington v. Patton*, 111 Wis. 208, 230, 86 N.W. 571 (1901)). In fact, advising the surviving spouse on the deferred marital property election may create a conflict of interest with the personal representative's duties. *See supra* § 12.51 (conflicts of interest).

➤ **Practice Tip.** The personal representative, or the personal representative's lawyer, may not be comfortable with representing the surviving spouse regarding the election. If this is the case, the surviving spouse may need to retain independent representation. The lawyer may wish to bring this situation to the attention of the personal representative in an engagement letter. For more discussion of potential conflicts of interest, see chapter 14, *infra*.

#### **4. Waiver of Right to Elect [§ 12.140]**

The surviving spouse may waive the right to make the deferred marital property election in whole or in part. Wis. Stat. § 861.10(1). The waiver may take place before the parties are married, during the marriage, or after the marriage has ended. *Id.* The waiver must be contained in a marital property agreement that is enforceable under section 766.58 or in a signed document described in section 861.08(1)(a) filed with a court after the decedent's death. *Id.* Unless the waiver provides otherwise, a waiver of "all rights" (or equivalent language) in the property or estate of a present or prospective spouse, or in a complete property settlement agreement entered into because of separation or divorce, is a waiver of the right to make the deferred marital property election. Wis. Stat. § 861.10(2).

#### **5. What Is Elected [§ 12.141]**

The surviving spouse has the right to elect "an amount equal to no more than 50% of the augmented deferred marital property estate." Wis. Stat. § 861.02(1); *see infra* §§ 12.148–.162 (augmented deferred marital property estate). Thus, the surviving spouse has the right to elect a pecuniary amount, not an interest in assets as under the prior election for deferred marital property assets subject to administration. The surviving spouse may elect less than a 50% amount.

## 6. Protection of Third Parties [§ 12.142]

If a beneficiary requests payment for a proportionate share of the elected amount, a third party who has received satisfactory proof of the decedent's death but has not received written notice that the surviving spouse has filed a petition for the deferred marital property elective share is not liable for (1) making a transfer to the beneficiary from property included in the augmented deferred marital property estate or (2) taking any other action in good-faith reliance on the validity of the governing instrument. Wis. Stat. § 861.11(2)(a).

For purposes of section 861.11, written notice of the surviving spouse's petition for the election must either (1) be mailed to the third party's main office or home by registered or certified mail, return-receipt requested, or (2) be personally served on the third party. Wis. Stat. § 861.11(3).

Upon receiving notice of the surviving spouse's petition, the third party may deposit any amount owed or any item of property with the probate court. Wis. Stat. § 861.11(4).

A financial institution as defined in section 705.01(3) is not liable for having transferred an account included in the augmented deferred marital property estate regardless of whether the financial institution received written notice of the surviving spouse's election petition. Wis. Stat. § 861.11(5)(b)(2). If a financial institution has reason to believe that a dispute exists with regard to the account, it may, but is not required to (1) deposit the funds in the account with the probate court as noted above, or (2) refuse to transfer the account to any person. Wis. Stat. § 861.11(5)(c). It is not clear whether the definition of *financial institution* in section 705.01(3) includes a life insurance company and brokerage house.

## 7. Equitable Election [§ 12.143]

Under the doctrine of equitable election, a beneficiary under a will may be required to choose between the benefits under the will and an asset that the testator is attempting to transfer. Wis. Stat. § 853.15; *see supra* § 12.23. A prior version of the equitable-election statute included exercise of the former deferred marital property election as a trigger of the equitable election. *See* Wis. Stat. § 853.15 (1995–96); *see also supra*

§ 12.24. Since the new deferred marital property election is of a pecuniary amount rather than an ownership interest in assets, the deferred marital property election is no longer a trigger of the equitable election. *See* 1997 Wis. Act 188, § 142 (amending section 853.15 to remove reference to deferred marital property election).

## **8. Nondomiciliary Surviving Spouse [§ 12.144]**

There is no requirement that the surviving spouse be domiciled in Wisconsin at the moment of the decedent spouse's death to make the deferred marital property election. The surviving spouse is eligible to make the deferred marital property election as long as the decedent was domiciled in Wisconsin at the time of death. Wis. Stat. § 861.02(7)(a).

➤ *Example.* A husband and wife are domiciled in Illinois. The husband moves to Wisconsin, and the wife stays behind in Illinois. The husband dies after having established a domicile in Wisconsin but before the wife establishes a domicile in Wisconsin. The wife may make the deferred marital property election.

## **9. Nondomiciliary Decedent [§ 12.145]**

If a decedent who was not domiciled in Wisconsin at the moment of death owned real property in Wisconsin, the right of the surviving spouse to make the deferred marital property election in that property is governed by section 861.20. Wis. Stat. § 861.02(7)(b). Section 861.20 provides that the surviving spouse has the same right to elect to take a portion of or interest in that real property as if the property were located in the decedent's domicile. The procedure of the decedent's domicile applies to the election.

➤ *Example.* Generally speaking, if an Illinois resident dies owning a summer home in Wisconsin, the surviving spouse's elective rights are governed by Illinois law.

## **10. Repeal of Grandfather Provision [§ 12.146]**

The prior augmented marital property estate election included a grandfather provision exempting certain nonprobate transfers from the

election. Specifically, the provision exempted nonprobate transfers for which the instrument of transfer was executed before April 4, 1984. Wis. Stat. § 861.05(4) (1995–96). 1997 Wisconsin Act 188, section 194, repealed the grandfather provision. Therefore, a number of assets exempt from the former augmented marital property estate election are now subject to the deferred marital property election.

➤ **Practice Tip.** Estate plans created in reliance on the grandfather provision should now be reexamined.

See chapter 1, *supra*, for a discussion of the constitutional implications of a retroactive change in legislation.

## **11. Tax Considerations [§ 12.147]**

A number of tax issues attend the deferred marital property election, such as the realization of capital gain if appreciated assets are used to fund the elected amount, the possibility that distribution of the elected amount to the surviving spouse might be deemed to carry out the estate's distributable net income to the surviving spouse, and so forth. See chapter 9, *supra*, for a discussion of the tax consequences attending the deferred marital property election.

### **C. Augmented Deferred Marital Property Estate [§ 12.148]**

#### **1. Definitions [§ 12.149]**

Section 861.02(2)(b) defines the augmented deferred marital property estate as follows:

The augmented deferred marital property estate is the total value of the deferred marital property of the spouses, irrespective of where the property was acquired, where the property was located at the time of a relevant transfer, or where the property is currently located, including real property located in another jurisdiction. It includes all types of property that fall within any of the following categories:

1. Probate and nonprobate transfers of the decedent's deferred marital property under s. 861.03(1) to (3).

2. Decedent's gifts of deferred marital property made during the 2 years before the decedent's death under s. 861.03(4).
3. Deferred marital property of the surviving spouse under s. 861.04.

➤ **Note.** The augmented deferred marital property estate is the total value of *both* spouses' deferred marital property, not just that of the decedent, as was the case under prior law.

*See also* Wis. Stat. § 861.018(1) (defining augmented deferred marital property estate by reference to section 861.02(2)).

Deferred marital property is defined in section 851.055 as any property that satisfies all the following requirements:

1. It is not classified by chapter 766.
2. It is not classified as individual property or marital property under a valid marital property agreement, unless the marital property agreement provides otherwise.
3. It was acquired while the spouses were married.
4. It would have been classified as marital property under chapter 766 if the property had been acquired when chapter 766 applied.

The amount of the surviving spouse's deferred marital property election is determined by creating a hypothetical estate (the augmented deferred marital property estate) analogous to the hypothetical estate created for purposes of determining federal and Wisconsin estate taxes. Items are excluded or included, valued, and then aggregated. When the final value of the hypothetical estate is known, it is multiplied by a percentage to determine the amount to which the surviving spouse is entitled. The full values of whole assets are included in the augmented deferred marital property estate. The percentage is used to replicate the value of the marital property interest.

➤ **Example.** If a decedent owned \$100,000 of deferred marital property, the surviving spouse owns no deferred marital property, and there are no adjustments, the surviving spouse has the right to elect an amount equal to 50% of \$100,000 or \$50,000.

## **2. What Is Included [§ 12.150]**

### **a. Decedent's Property [§ 12.151]**

#### **(1) Deferred Marital Property in Decedent's Probate Estate [§ 12.152]**

The augmented deferred marital property estate includes the value of deferred marital property in the decedent's probate estate. Wis. Stat. § 861.03(1). The term *probate estate* is not defined. Technically, the term applies only to estates for which a will has been admitted to probate. However, it is apparent that the term is intended to apply to all estates subject to administration, including intestate estates and estates for which a will has been admitted to probate.

#### **(2) Deferred Marital Property Passing By Nonprobate Means at Decedent's Death [§ 12.153]**

The augmented deferred marital property estate includes the value of deferred marital property owned or owned in substance by the decedent immediately before death that passed outside probate at the decedent's death. Wis. Stat. § 861.03(2). These items include the following:

1. The decedent's fractional interest in deferred marital property that was held by the decedent with the right of survivorship;
2. The decedent's ownership interest in deferred marital property that was held by the decedent in a form payable or transferable on death, including deferred employment benefits, individual retirement accounts, annuities, and transfers under marital property agreements or in co-ownership with the right of survivorship;
3. Deferred marital property in the form of proceeds of insurance on the decedent's life, including accidental death benefits, that were payable at the decedent's death, if the decedent owned the insurance policy immediately before death or if the decedent alone and immediately before death held a presently exercisable general power of appointment over the policy or its proceeds; and

4. Deferred marital property over which the decedent alone, immediately before death, held a presently exercisable general power of appointment, to the extent that the property passed at the decedent's death by exercise, release, lapse, default, or otherwise.

*Id.*

### **(3) Deferred Marital Property Transferred with Retained Rights or Benefits [§ 12.154]**

The augmented deferred marital property estate includes the value of any deferred marital property transferred by the decedent in which the decedent retained rights or benefits. Wis. Stat. § 861.03(3). These items include the following:

1. Deferred marital property in which the decedent retained the right to possession, use, enjoyment, or income and that was irrevocably transferred, to the extent that the decedent's right terminated at death or continued beyond death;

➤ **Note.** A grantor-retained annuity trust, commonly known as a GRAT, would be included in this category if the grantor died before the expiration of the annuity. A qualified personal-residence trust, commonly known as a QPRT, would also be included, if the grantor died before the expiration of the retained term.

2. Deferred marital property in which the decedent retained the right, either alone or in conjunction with any person: (1) to designate the persons who are to possess or enjoy the property or the income from the property, (2) to control the time at which designated persons are to possess or enjoy the property or income from the property, or (3) to alter or amend the terms of the property transfer, to the extent that the decedent's right terminated at death or continued beyond death; and
3. Any transfer of deferred marital property, including the transfer of an income interest, in which the decedent created a power of appointment, including the power to revoke or terminate the transfer



or to consume, invade, or dispose of the principal or income, if the power was exercisable by the decedent alone, by the decedent in conjunction with another person, or by a nonadverse party, and if the power is for the benefit of the decedent, the decedent's creditors, the decedent's estate, or creditors of the decedent's estate.

*Id.*

#### **(4) Deferred Marital Property Transferred Within Two Years of Death [§ 12.155]**

The augmented deferred marital property estate includes the value of any deferred marital property transferred by the decedent within two years of death. Wis. Stat. § 861.03(4). These items include the following:

1. Deferred marital property that passed as a result of the termination of the right or interest in, or power of appointment over, property that would otherwise have been included in the augmented deferred marital property estate;
2. Transfers of or relating to the deferred marital property component of a life insurance policy on the decedent's life if the proceeds would otherwise have been included; and
3. Any transfer of deferred marital property to the extent that it is not otherwise included in the augmented deferred marital property estate, but only if the aggregate transfers to any one donee in either of the two years exceed \$10,000.

*Id.*

#### **b. Surviving Spouse's Property [§ 12.156]**

##### **(1) In General [§ 12.157]**

Under section 861.04, the augmented deferred marital property estate includes the value of any deferred marital property that would have been included in the augmented deferred marital property estate had the

surviving spouse been the decedent. Wis. Stat. § 861.04(1). When applying section 861.04(1), it is necessary to determine whether the surviving spouse is treated as dying before or after the decedent because the order of deaths of spouses affects property interests under the marital property law.

Section 861.04(2m) provides that “[w]hen the surviving spouse is treated as the decedent under sub. (1), the decedent is not treated as the surviving spouse for the purposes of s. 861.05(1)(e) or (2m).”

Section 861.05(2m)(a) provides in part that “[t]he surviving spouse shall be treated as having died after the decedent on the date of the decedent’s death....”

Section 861.04(2m) implies that the surviving spouse is treated as dying before the decedent except for the stated exceptions. Section 861.05(2m)(a) expressly provides that the surviving spouse is treated as dying after the decedent. Notwithstanding section 861.04(2m), it appears that section 861.05(2m)(a) will apply in most cases..

The following example illustrates the determination of the property belonging to the surviving spouse that is included in the augmented marital property estate.

➤ **Example.** A husband dies on June 30, 2008, survived by his wife. The husband’s only nonmarital property asset is a certificate of deposit (CD) with a value of \$100,000. The CD is deferred marital property. His wife owns two items of nonmarital property that were deferred marital property. The first is a term life insurance policy insuring her life with a death benefit of \$100,000 and a value on the date of her husband’s death of \$50, the amount of the unearned premium. Her second item of nonmarital property is a 401(k) plan having a value on the date of her husband’s death of \$100,000.

In the above example, the value of the husband’s CD for purposes of determining the value of the augmented deferred marital property estate is clear: \$100,000. However, the value of the life insurance and the 401(k) plan require some analysis.

## **(2) Life Insurance [§ 12.158]**

Section 861.05 prescribes valuation methods for valuing the decedent's property and the surviving spouse's property to be included in the augmented deferred marital estate. Section 861.05(2) describes how the decedent's property is valued. Section 861.05(2m) describes how the surviving spouse's property is valued.

Section 861.05(2m)(b) has a special valuation rule for life insurance insuring the surviving spouse. Therefore, it is not necessary to determine whether the surviving spouse is treated as dying before or after the decedent. The special rule provides that the value of the term life insurance policy is the unearned premium, which is \$50 in the example.

## **(3) 401(k) Plan [§ 12.159]**

The 401(k) plan in the example is not marital property, but the example does not indicate whether it is deferred individual property or deferred marital property.

If it is deferred individual property, it is not necessary to determine whether the surviving spouse died before or after the decedent. The value is \$100,000 for purposes of inclusion in the augmented deferred marital property estate.

If it is deferred marital property, it is necessary to determine whether the surviving spouse is treated as dying before or after the decedent. If the survivor is treated as dying before the decedent, the value is \$100,000. However, if the survivor is treated as dying after the decedent, the terminable-interest rule in section 766.62(5) may apply. Under that rule, the marital property interest of the nonemployee spouse in a retirement plan terminates if the nonemployee dies first. Section 861.05(2m)(a) provides that the surviving spouse is treated as surviving the decedent, and so if the terminable interest rule is applied, the value is \$0 for purposes of inclusion. If the terminable-interest rule is not applied, the value is \$100,000. The Probate Code Drafting Committee intended that the terminable interest be applied. Erlanger, *supra* § 12.137, app. C at 44.

An issue that arises with respect to the 401(k) plan is federal preemption of ERISA. In *Boggs v. Boggs*, 520 U.S. 833 (1997), the U.S.

Supreme Court ruled that, in certain circumstances, state community property laws that would otherwise apply to retirement benefits are preempted by federal law. The application of *Boggs v. Boggs* generally is uncertain. *See supra* §§ 9.67, 10.136. One view of the *Boggs* case is that the nonemployee spouse (the husband in our example) has a marital property interest in the 401(k) plan but is unable to make a disposition of the interest if he predeceases the employee spouse. Under that view, Wisconsin can include the value of the 401(k) plan in the augmented deferred marital estate.

A second view of the *Boggs* decision is that the nonemployee spouse can have no community property interest at all. Under that view, the wife's 401(k) plan would be deferred individual property, not deferred marital property, and would not be in the augmented deferred marital property estate.

The better view is that the doctrine of preemption does not prevent the 401(k) plan from being deferred marital property for purposes of the deferred marital property election.

Section 861.07(4) provides that the recipient of deferred marital property is still personally liable to the spouse if an asset is included in the augmented marital property estate but cannot pass to the recipient because of federal preemption. Apparently, being designated a recipient is enough to create personal liability even though no property actually passed to the designated recipient.

### **3. What Is Excluded [§ 12.160]**

The augmented deferred marital property estate excludes the following:

1. Transfers of deferred marital property to the extent that the decedent received full or partial consideration for the transfer in money or money's worth;
2. Transfers under the Social Security system;
3. Transfers of deferred marital property to third persons with the written joinder or written consent of the surviving spouse; and

4. Transfers of deferred marital property to the surviving spouse under section 861.33 (selection of personalty) or section 861.41 (exempt property).

Wis. Stat. § 861.05(1).

If the same property could be included in the augmented deferred marital property estate more than once, the property is included only once under the provision that yields the greatest value. Wis. Stat. § 861.05(4).

➤ **Note.** The above exclusions are the articulated exclusions. The application of federal preemption may result in other exclusions. Assets that might be affected by federal preemption include federal veterans' benefits, railroad retirement benefits, military retirement benefits, disability benefits, civil service retirement benefits, foreign service retirement benefits, and private retirement plan benefits. *See supra* § 2.213.

#### **4. Valuation of Included Items [§ 12.161]**

Section 861.05(2) provides valuation rules for valuing the decedent's property included in the augmented deferred marital property estate. These rules include the following:

1. Section 861.05(2)(a) provides that certain assets—for example, probate assets and life insurance—are valued as of the decedent's date of death. Thus, if the decedent died on June 30, the assets are valued as of June 30.
2. Section 861.05(2)(b) provides that certain assets—deferred employment benefits and IRAs—are valued as of immediately before the decedent's death.
3. Section 861.05(2)(c) provides that certain assets are valued as of the date the decedent's right, interest, or power terminated.
4. Section 861.05(2)(d) provides that gifts of deferred marital property within two years of the decedent's death are valued as of the date of the transfer.

Section 861.05(2m) provides valuation rules for valuing the surviving spouse's property included in the augmented marital property estate. The surviving spouse's property is valued in the same manner as the decedent's property, with two exceptions. Section 861.05(2m)(a) provides that the surviving spouse will be treated as having died after the decedent on the date of the decedent's death. Section 861.05(2m)(b) has a special rule for valuing life insurance insuring the surviving spouse that, in effect, treats the surviving spouse as having died before the decedent.

## **5. Expenses [§ 12.162]**

Section 861.05(3) provides that the value of deferred marital property included in the augmented deferred marital property estate is to be reduced by "an equitable proportion" of funeral and burial expenses, administrative expenses, other charges and fees, and enforceable claims. The statute does not define the word *equitable*.

➤ **Comment.** A number of practical questions will arise under section 861.05(3). For example, should charges relating to probate assets be chargeable only against probate assets? Should the financial or other circumstances of the decedent and the surviving spouse be taken into account?

➤ **Note.** An amount elected under the deferred marital property election is subject to equitable reduction under section 861.05(3) although it may be excepted from abatement under section 854.18. Section 854.18 provides for abatement of probate and nonprobate assets but excepts the elective share amount of a surviving spouse who elects under section 861.02."

## **D. Satisfaction and Collection of Amount Elected [§ 12.163]**

### **1. In General [§ 12.164]**

If a surviving spouse makes an election under section 861.02, the probate court determines, after notice and hearing, the deferred marital property elective-share amount and the property that satisfies that

amount. Wis. Stat. § 861.08(5)(a). If the personal representative does not hold the money or property included in the augmented deferred marital property estate, the court determines the liability of any person or entity that has any interest in the money or property or that holds the money or property. Wis. Stat. § 861.08(5)(b).

The initial order of satisfaction of the elective-share amount is prescribed as follows:

1. All property included in the augmented deferred marital property estate belonging to the surviving spouse;
2. All marital property, individual property, deferred marital property, or deferred individual property transferred to the surviving spouse from the decedent; and

➤ **Note.** The following are excepted from this second rule: (a) transfers under section 861.33 (selection of personalty) and section 861.41 (exemption of property); (b) transfers under section 861.31 (family allowances) or section 861.35 (special allowance), unless the court orders otherwise; and (c) transfers under the Social Security system.

3. All gifts to the surviving spouse during the decedent's lifetime, except the first \$5,000 of gifts each year and gifts received from the decedent that the surviving spouse can show were subsequently and gratuitously transferred in a manner that, had they been the deferred marital property of the surviving spouse, would not have been included in the augmented deferred marital property estate under section 861.04.

Wis. Stat. § 861.06(2).

After the above property has been applied toward satisfaction, the remainder of the elective-share amount is to be satisfied proportionally from transfers to persons other than the surviving spouse of property included in the augmented deferred marital property estate by reason of section 861.03(1), (2), (3), or (4)(b)2. Wis. Stat. § 861.06(3).

Finally, after the above property has been applied, the remainder of the elective-share amount is to be satisfied proportionally from transfers

to persons other than the surviving spouse of property included under section 861.03(4)(b)1. or 3. Wis. Stat. § 861.06(4).

If all or a part of a prorated share is uncollectible, the court may increase the prorated liability of recipients if the court finds that an equitable adjustment is necessary to avoid hardship. Wis. Stat. § 861.06(5). No recipient or donee of a recipient is liable for an amount greater than the value of the deferred marital property received. Wis. Stat. § 861.06(5)(b).

## **2. Jurisdictional Considerations [§ 12.165]**

Satisfaction of the augmented deferred marital property elected amount by third-party recipients will occur in two contexts: from property subject to the probate court's jurisdiction and from property not subject to the probate court's jurisdiction. Presumably, if a recipient is adjudicated to be personally liable to the surviving spouse and the personal representative holds assets to which the recipient is entitled, there can be an offset. However, if a third-party recipient is not entitled to property under the probate court's jurisdiction and does not submit to the probate court's jurisdiction, collection may be difficult. The following example is derived from *Jackson v. Employee Trust Funds Board*, 230 Wis. 2d 677, 602 N.W.2d 543 (Ct. App. 1999).

➤ **Example.** A spouse designated her sister in Wisconsin as the beneficiary of the \$500,000 death benefit of a life insurance policy insuring the spouse. The spouse died, and the surviving spouse filed a petition for the deferred marital property election. The proceeds of the life insurance policy are deferred marital property. Assume that under section 861.07 (personal liability of recipients), the prorated amount for which the sister in Wisconsin is personally liable is \$250,000. Assume the sister in Wisconsin received notice of the hearing on the election petition as required by section 861.08(2).

The mailing of a notice to the Wisconsin sister does not give the Wisconsin probate court jurisdiction over the sister if the sister is not entitled to property under the Wisconsin probate court's jurisdiction. At a minimum, a summons and complaint from a Wisconsin circuit court will be necessary for a Wisconsin court to have jurisdiction over the sister. The circuit court will be the court that adjudicates the sister's personal liability under section 861.07.



If the sister lives in California instead of Wisconsin, obtaining jurisdiction over the sister may be more difficult. Also, a California court may make the adjudication of personal liability.

The mailing of a notice to a California resident does not give the Wisconsin probate court jurisdiction over the California resident if the California resident is not entitled to property under the Wisconsin probate court's jurisdiction. At a minimum, a summons and complaint from a Wisconsin circuit court will be necessary for a Wisconsin court to have jurisdiction over the sister. However, if the sister has no contacts with Wisconsin, the Wisconsin circuit court may not be able obtain jurisdiction under Wisconsin's long-arm statute, section 801.05.

If the Wisconsin courts do not have jurisdiction over the sister, the action must be filed in California. The California court may choose not to apply the Wisconsin statute, section 861.07, that imposes personal liability on transfer recipients. The California court may choose to apply California law and hold that under California law, the beneficiary is entitled to death benefits of life insurance policies.

#### **E. Assignment of Home to Surviving Spouse [§ 12.166]**

If a married decedent had a property interest in a home, whether marital property or nonmarital property, the decedent's entire interest in the home is assigned to the surviving spouse if (1) the surviving spouse petitions the court requesting such a distribution, and (2) the governing instrument does not provide a specific transfer of the decedent's interest to someone else. Wis. Stat. § 861.21(2). The surviving spouse must file the petition within six months after the decedent's death, unless the court extends the time for filing. *Id.* The surviving spouse must pay for the value of the interest being assigned to the spouse. *See* Wis. Stat. § 861.21(4).

#### **F. Allowances for Support of Spouse, Domestic Partner, and Dependent Children [§ 12.167]**

Section 861.31 permits the probate court to order an allowance for the support of the surviving spouse, surviving domestic partner, and any minor children during the administration of the estate. Section 861.35 permits the probate court to order a special allowance for the support and

education of each minor child and for the support of the surviving spouse or surviving domestic partner after administration of the estate has terminated.

### **G. Rights in Property Transferred in Fraud of Surviving Spouse [§ 12.168]**

Section 861.17, governing rights in property transferred in fraud of the surviving spouse, predates the Wisconsin Marital Property Act. *See* ch. 339, Laws of 1969 (eff. Apr. 1, 1971). Section 861.17(1) provides that nothing in chapter 861 precludes a court from subjecting any property arrangement made by the decedent in fraud of the survivor's rights to the rights of the surviving spouse. A property arrangement in fraud of those rights is defined as "[a]ny transfer or acquisition of property, regardless of the form or type of property rights involved, made by the decedent during marriage or in anticipation of marriage for the primary purpose of defeating the rights of the surviving spouse" under

1. Chapter 852 (intestacy), or
2. Chapter 861 (family rights).

Wis. Stat. § 861.17(1).

➤ *Query.* The reason for the inclusion of intestacy is unclear. What rights of intestacy does the surviving spouse have? Section 861.17(1)(a) applies to all types of property: marital property, individual property, and predetermination date property. Under section 861.01, after the death of the predeceasing spouse, the surviving spouse and the decedent's successor each own an undivided one-half interest in former marital property as tenants in common. If the decedent dies intestate and there are children, all of whom are children of the decedent and the surviving spouse, the surviving spouse inherits the decedent's entire estate. Wis. Stat. § 852.01(1)(a). If the decedent chooses not to have a will and gives individual property and predetermination date property (which is not deferred marital property) to the children during his or her lifetime, might such a transfer be subject to section 861.17?

Arrangements that provide for the issue of a prior marriage and that were made before marriage, within one year after marriage, or before April 1, 1971, are not fraudulent property arrangements for purposes of section 861.17. Wis. Stat. § 861.17(2).

A surviving spouse's recovery under section 861.17 is limited to the share the spouse would receive under chapters 852 and 861. Wis. Stat. § 861.17(3). In addition to any recovery under section 861.17, the spouse may retain any assets passing to him or her as a result of the death of the predeceasing spouse, including any property received from the probate estate and any property passing to the surviving spouse under the fraudulent arrangement.

## **XII. Conflicts of Laws [§ 12.169]**

A spouse domiciled in a common-law property state or community property state may die owning property located in Wisconsin. Conversely, a spouse domiciled in Wisconsin may die owning property in another common-law property state or community property state. For a discussion of the treatment of this property under conflict-of-law principles, see chapter 13, *infra*.

## **XIII. Summary Procedures [§ 12.170]**

### **A. In General [§ 12.171]**

The Probate Code contains three summary procedures for the confirmation of the nontestamentary vesting of property with a right of survivorship or the transfer of property subject to a nontestamentary disposition provision of a marital property agreement. These procedures may also be used to confirm the surviving spouse's interest in former marital property. The three summary procedures are (1) section 867.046(1m) (a judicial proceeding), (2) section 867.046(2) (an administrative proceeding before the register of deeds), and (3) section 865.201 (informal administration).

## **B. Survivorship Marital Property and Spousal Joint Tenancy: Summary Judicial Proceeding [§ 12.172]**

Section 867.046(1m) permits a decedent's spouse to petition the probate court for a certificate setting forth the facts of death, the termination or transfer of the decedent's interest in the property, the petitioner's interest in the property, and any other facts essential to a determination of the rights of persons interested. Uniform Probate Form PR-1929 is used for this petition. Probate forms can be downloaded from the Wisconsin Court System Web site at <http://www.wicourts.gov/forms1/circuit.htm#probate>.

## **C. Washington Will Provisions: Summary Judicial Proceeding [§ 12.173]**

Section 867.046(1m) permits the beneficiary of a marital property agreement to petition the probate court for a certificate setting forth the facts of death, the termination or transfer of the decedent's interest in the property, the interest of the petitioner in the property, and any other facts essential to a determination of the rights of persons interested. At present, there is no uniform form for a petition the court to confirm dispositions under a marital property agreement, pursuant to section 766.58(3)(f), the Washington will provision. However, there is a uniform form for use in informal administration, PR-1812. There is a form of petition and certificate for formal administration at Mark J. Bradley et al., *Eckhardt's Workbook for Wisconsin Estate Planners* §§ 7.36–.37 (5th ed. 2008).

In *Maciolek v. City of Milwaukee Employees' Retirement System Annuity & Pension Board*, 2006 WI 10, 288 Wis. 2d 62, 709 N.W.2d 360, the supreme court affirmed the court of appeals' holding that the pension board had the right to insist on a judicial confirmation proceeding under section 867.046(1m) before transferring assets pursuant to a Washington will provision of a marital property agreement. The retirement plan did not give the participant an opportunity to designate a beneficiary. Thus, the proceeds were part of the participant's estate subject to administration.

In response to *Maciolek*, the legislature amended the definition of governing instrument under section 854.23 to include all instruments

described in section 854.01. This added the Washington will provision of chapter 766 (section 766.58(3)(f)) to the payer-protection provisions of section 854.23. Including Washington wills within the payer-protection provisions may induce a payer to forgo a summary confirmation proceeding under section 867.046(1m). However, under the holding of the *Maciolek* decision, payers may still require summary confirmation procedures before agreeing to transfer property pursuant to a Washington will provision.

#### **D. HT-110: Administrative Proceeding Before County Register of Deeds [§ 12.174]**

Section 867.046(2) permits a decedent's spouse or the beneficiary of a marital property agreement to obtain evidence of the termination of the decedent's interest in certain property and confirmation of the petitioner's interest in the property. The statute provides for an administrative procedure involving the county register of deeds. Form HT-110, published by the Wisconsin Register of Deeds Association, is used for this proceeding. Form HT-110 may be downloaded from the Wisconsin Register of Deeds Association Web site at <http://www.wrdaonline.org/forms/index.htm>. This administrative proceeding before the register of deeds applies to real property, a vendor's interest in a land contract, an interest in a savings or checking account, an interest in a security, or a mortgagee's interest in a mortgage. Form HT-110 may be used for transfers of survivorship marital property and for dispositions under marital property agreements.

In *Maciolek v. City of Milwaukee Employees' Retirement System Annuity & Pension Board*, 2006 WI 10, 288 Wis. 2d 62, 709 N.W.2d 360, the supreme court affirmed the court of appeals' holding that the summary procedure under section 867.046(2) did not apply to an interest in the city of Milwaukee retirement plan. The retirement plan did not provide the participant an opportunity to designate a beneficiary. Thus, the proceeds were part of the participant's estate subject to administration.

In response to *Maciolek*, the legislature amended the definition of governing instrument under section 854.23 to include all instruments described in section 854.01. This added the Washington will provision of chapter 766 (section 766.58(3)(f)) to the payer protection provisions of section 854.23. Including Washington wills to the payer protection

provisions may induce a payer to forgo a summary confirmation proceeding under section 867.046(1m). However, under the holding of the *Maciolek* case, payers may still require summary confirmation procedures before agreeing to transfer property pursuant to a Washington will provision.

### **E. Survivorship Marital Property and Spousal Joint Tenancy: Summary Informal Proceeding [§ 12.175]**

Section 865.201 provides that the personal representative may file with the probate registrar a verified statement describing property in which the decedent had an interest in marital property or in which any designated person, trust, or other entity has an interest passing by nontestamentary disposition under section 766.58(3)(f), including the recording data, if any, of the document creating the interest and any right of survivorship.

Upon filing, the statement constitutes prima facie evidence of the facts recited and evidences the termination of the decedent's interest and the confirmation of the surviving spouse's or the designated person's trust's or other entity's interest in the property listed, with the same effect as if a certificate had been issued by the court under section 867.046.

Uniform Probate Form PR-1812 is used for this Statement in Informal Administration. Form PR-1812 includes nontestamentary dispositions pursuant to section 766.58(3)(f), the Washington will provision. Form PR-1929, used for formal administration, does not include Washington will dispositions. However, there is a form of petition and certificate for formal administration at Mark J. Bradley et al., *Eckhardt's Workbook for Wisconsin Estate Planners* §§ 7.36–.37 (5th ed. 2008).

## **XIV. Closing Estates [§ 12.176]**

### **A. In General [§ 12.177]**

Section 863.27 permits the final judgment in the probate of an estate to confirm the nontestamentary vesting of a decedent's interest in

survivorship marital property and the nontestamentary transfer of the decedent's interest in property by marital property agreement.

While in the estate, net probate income is not marital property even though the beneficiary who will ultimately receive the income is married. However, income distributed from estates to a married beneficiary is marital property. Wis. Stat. § 766.01(10); *see supra* § 2.85.

➤ **Practice Tip.** Since net probate income may be marital property upon receipt by a married beneficiary but assets inherited by the beneficiary are individual property, the personal representative may wish to consider separate distributions of income and principal to the beneficiary. If the personal representative combines income and principal in one distribution, the beneficiary will receive a mixed asset. It will be easier for the beneficiary to keep the inherited assets classified as individual property if separate distributions are received. Also, the beneficiary may wish to consider executing a unilateral statement classifying the income as individual property before the income is distributed. *See supra* §§ 2.70–.82.

## **B. Exchanges of Interests in Former Marital Property**

### **[§ 12.178]**

Wisconsin adopted an item-by-item marital property rule instead of an aggregate rule. Wis. Stat. § 861.01; *see supra* §§ 2.22, 10.10. Under the item-by-item rule, after the death of one spouse, the surviving spouse owns an undivided one-half interest in every item of former marital property. Therefore, after the death of one spouse, the surviving spouse and the beneficiaries of the predeceasing spouse will own the former marital property as tenants in common. The surviving spouse and the beneficiaries may wish to exchange their undivided interests among themselves so that each person owns an entire asset.

➤ **Query.** If the surviving spouse and the decedent's beneficiaries agree to an exchange, is the transaction taxable for federal and Wisconsin income tax purposes? Two private letter rulings have held that a division of community property after the death of one spouse is not a taxable exchange. *See* Priv. Ltr. Rul. 8037124 (June 23, 1980), 8016050 (Jan. 23, 1980).

Section 766.31(3)(b)3. provides a procedure by which the surviving spouse and another person who succeeds to all or part of the decedent's one-half interest in marital property may petition the court to approve an exchange of interests in the marital property. The exchange must

1. Occur before the final distribution of the estate;
2. Be composed of items that are fairly representative of the appreciation and depreciation occurring since the decedent's death;
3. Be composed of items having a fair market value at the time of the exchange equal to what would have been distributed had no exchange request been made, including any money used in the exchange; and
4. Be reported in writing to the Wisconsin Department of Revenue (currently, there is no form for such reporting).

➤ **Comment.** Presumably, the above procedure is permissive and not exclusive. The Legislative Council Committee Note to section 857.03(2) (renumbered to 766.31(3)(b)3.) indicates that the procedure does not bind the IRS. *See* Wis. Stat. Ann. § 857.03(2) Legis. Council Comm. Notes—1987 Act 393 (West. 2002); *see also supra* chs. 9 and 10 (additional discussions of exchange procedure).

## **XV. Guardians and Wards [§ 12.179]**

A guardian of the estate of an incompetent spouse may exercise, with the approval of the probate court, any management and control right over property and any right in the business affairs that the married person could exercise if competent. Wis. Stat. § 54.20(2)(h). The guardian may consent to “act together in or join in” any transaction for which consent or joinder of both spouses is required. Furthermore, the guardian may execute a marital property agreement with the other spouse but may not make, amend, or revoke a will. *Id.* These powers are in addition to powers otherwise provided for guardians of the estate. *See* Wis. Stat. § 54.20.



## Conflict of Laws

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**I. Scope of Chapter [§ 13.1]**

This chapter examines the issues that arise when courts must determine whether to apply Wisconsin's marital property law or the common law property system of another state in a particular case. The general concepts and rules of conflict-of-laws jurisprudence are discussed, along with the rules that apply specifically to property. The chapter then discusses the application of choice-of-laws principles to the classification of property owned by spouses both in and outside of Wisconsin, including issues related to death, divorce, creditors' claims, marriage agreements, and tort causes of action and recoveries.<sup>1</sup>

**II. General Conflict-of-laws Principles [§ 13.2]**

**A. Basic Concepts and Rules [§ 13.3]**

Conflict of laws is a relatively specialized area of jurisprudence involving cases with a significant relationship to more than one state. Because the Wisconsin Marital Property Act, 1983 Wisconsin Act 186 (codified as amended at chapter 766 and scattered sections of the Wisconsin Statutes) [hereinafter the Act or the Wisconsin Marital Property Act], differs significantly from the substantive law of states with common law property systems, and because the American population is increasingly mobile, cases involving the application of conflict-of-laws rules to property interests of spouses will increasingly occur. These rules will be applied not only when married persons move

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<sup>1</sup> Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2007–08 Wisconsin Statutes, as amended by acts through 2009 Wisconsin Act 189, and all references to the United States Code (U.S.C.) are current through Public Law No. 111-160 (excluding Pub. L. Nos. 111-148, 111-152, 111-159) (Apr. 26, 2010). Textual references to the Wisconsin Statutes are indicated as “chapter xxx” or “section xxx.xx,” without the designation “of the Wisconsin Statutes.”

into or out of Wisconsin but also when spouses residing in common law property jurisdictions acquire property in Wisconsin and when spouses residing in Wisconsin use marital property to acquire property elsewhere.

Conflict-of-laws rules in the broadest sense cover such areas as judicial jurisdiction and competence—that is, rules relating to the ability of the courts of a state where an action is commenced (the forum state) to exercise jurisdiction when the suit involves incidents that occurred elsewhere or persons who are not physically present in the forum jurisdiction. Additionally, conflict-of-laws rules include rules regarding the effect that the courts in one state will give to judgments rendered in another. Lastly, conflict-of-laws rules include rules to determine choice of the law to be applied in resolving the rights and liabilities that flow from a transaction or occurrence when parts of it are connected with states other than the forum state. Restatement (Second) of Conflict of Laws § 2 (1971) (revised 1989) [hereinafter Restatement]. In practice, the term *conflict of laws* is often used as a synonym for *choice of laws* instead of being correctly applied to the broader array of conflict-of-laws rules.

In a case involving a significant relationship to more than one state, choice-of-laws considerations are at the heart of conflict-of-laws jurisprudence. The use of choice-of-laws rules rests on a determination that fairness and justice dictate applying all or part of the law of another state to resolve a controversy with multistate ramifications, rather than simply applying the law of the forum jurisdiction in its totality or refusing to hear the case in the forum state at all. Application of choice-of-laws principles necessarily involves weighing and balancing the potentially different policies and interests of the states affected by the transaction and entails considerable judicial subjectivity about which legal principles should be emphasized in resolving the dispute. The Restatement points out that the conflict-of-laws rules, especially those relating to choice of laws, are normally decisional, and thus, like other common law rules, are subject to periodic re-examination. Restatement § 5.

The choice-of-laws principles as set forth in Restatement section 6 illustrate the broad inquiry courts face in resolving conflict-of-laws questions:

§ 6. Choice-of-Law Principles

(1) A court, subject to constitutional restrictions, will follow a statutory directive of its own state on choice of law.

(2) When there is no such directive, the factors relevant to the choice of the applicable rule of law include

- (a) the needs of the interstate and international systems,
- (b) the relevant policies of the forum,
- (c) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue,
- (d) the protection of justified expectations,
- (e) the basic policies underlying the particular field of law,
- (f) certainty, predictability and uniformity of result, and
- (g) ease in the determination and application of the law to be applied.

**B. Wisconsin Conflict-of-laws Rules [§ 13.4]**

**1. Concept of Choice-influencing Considerations  
[§ 13.5]**

In *Heath v. Zellmer*, 35 Wis. 2d 578, 151 N.W.2d 664 (1967), the Wisconsin Supreme Court adopted a conflict-of-laws methodology developed by Professor Robert A. Leflar. See Robert A. Leflar, *Choice-Influencing Considerations in Conflicts Law*, 41 N.Y.U. L. Rev. 267 (1966); Robert A. Leflar, *Conflicts Law: More on Choice-Influencing Considerations*, 54 Cal. L. Rev. 1584 (1966); see also Robert A. Leflar et al., *American Conflicts Law* (4th ed. 1986). The methodology analyzes five choice-influencing considerations:

1. Predictability of results;
2. Maintenance of interstate and international order;
3. Simplification of the judicial task;
4. Advancement of the forum's governmental interests; and
5. Application of the better rule of law.

Although these considerations are more abbreviated than the considerations in Restatement section 6, discussed at section 13.3, *supra*, they contain most of the same elements.

In commenting on these five choice-influencing considerations, the court in *Heath* pointed out that the first consideration, predictability of results, deserves special emphasis in consensual arrangements and in those involving property rights:

Predictability is an essential in the law of wills, descent and distribution, trusts, contracts, land titles, and conveyancing. It has little or no relevancy to ... [a] tort that was never intended or planned.

35 Wis. 2d at 596.

According to the court, the second consideration, maintenance of interstate order, means

that no state should impose its law in a situation when its parochial rules would unduly and without substantial reason so impinge upon another state as to interfere with the free flow of commerce or the exercise of another state's legitimate policies in such a manner that would invite retaliation from another jurisdiction. Deference to the substantial interests of another state are necessary and for a state that is only minimally concerned with a transaction or tort to thrust its law upon the parties would be disruptive of the comity between states.

*Id.*

As to the third consideration, simplification of the judicial task, the court explained that

a court will not lightly consider a rule that will complicate its task or make the process of case deciding more onerous for itself or for the bar of its state. A simple and easily applied rule of substantive or procedural law is to be preferred, but simplicity may well be outweighed by other considerations.

*Id.* at 597.

The court said that the fourth consideration, advancement of the forum's governmental interests, would not necessarily be achieved through slavish application of the law of the forum but rather by ascertaining "whether the proposed nonforum rule comports with the standards of fairness and justice that are embodied in the policies of the forum law." *Id.* at 598.

Finally, the court described the fifth consideration, application of the better rule of law, as being at the heart of common law decision-making: “If the way is open to them, courts will select the law that most adequately does justice to the parties and has the greatest likelihood of being applicable with justness in the future.” *Id.* The court saw the choice of better law as an objective one, grounded “not upon preferred parties but upon preferred law.” *Id.* at 599.

Wisconsin courts have applied the analytical model in *Heath* primarily in tort cases, *see, e.g., Hunker v. Royal Indem. Co.*, 57 Wis. 2d 588, 204 N.W.2d 897 (1973); *Conklin v. Horner*, 38 Wis. 2d 468, 157 N.W.2d 579 (1968); *Zelinger v. State Sand & Gravel Co.*, 38 Wis. 2d 98, 156 N.W.2d 466 (1968), but also in contract cases, *see, e.g., Schlosser v. Allis-Chalmers Corp.*, 86 Wis. 2d 226, 271 N.W.2d 879 (1978); *Air Prods. & Chems., Inc. v. Fairbanks Morse, Inc.*, 58 Wis. 2d 193, 206 N.W.2d 414 (1973); *Haines v. Mid-Century Ins. Co.*, 47 Wis. 2d 442, 177 N.W.2d 328 (1970). Nevertheless, the analytical model of *Heath* is not used in every situation. The courts have noted that sometimes a state’s connection to a case may be so obviously limited or minimal that the detailed conflicts analysis described in *Heath* is not necessary. *Hunker*, 57 Wis. 2d at 598; *Gavers v. Federal Life Ins. Co.*, 118 Wis. 2d 113, 118, 345 N.W.2d 900 (Ct. App. 1984). *But see Beloit Liquidating Trust v. Grade*, 2004 WI 39, ¶¶ 24–25, 270 Wis. 2d 356, 677 N.W.2d 298. In this event, the law of the state with the great majority of contacts is applied.

## 2. Concept of “Grouping-of-Contacts” [§ 13.6]

In several post-*Heath* conflict-of-laws cases involving contracts, the Wisconsin Supreme Court has used the *grouping-of-contacts* or *center-of-gravity* approach embodied in Restatement section 188 as the primary vehicle to resolve choice-of-laws questions. *Desert Palace, Inc. v. Jafari (In re Jafari)*, 385 B.R. 262 (W.D. Wis. 2008); *State Farm Mut. Auto. Ins. Co. v. Gillette*, 2002 WI 31, ¶ 26, 251 Wis. 2d 561, 641 N.W.2d 662; *Handal v. American Farmers Mut. Cas. Co.*, 79 Wis. 2d 67, 74, 255 N.W.2d 903 (1977); *Haines*, 47 Wis. 2d at 446–47; *Urhammer v. Olson*, 39 Wis. 2d 447, 450, 159 N.W.2d 688 (1968); *American Family Mut. Ins. Co. v. Powell*, 169 Wis. 2d 605, 609, 486 N.W.2d 537 (Ct. App. 1992). This approach is used in conjunction with the choice-influencing considerations outlined in *Heath*. *Schlosser*, 86 Wis. 2d at 239–40; *Air Prods.*, 58 Wis. 2d at 202–03; *Haines*, 47 Wis. 2d at 446–47, 451.

The Restatement's grouping-of-contacts rule states as follows:

§ 188. Law Governing in Absence of Effective Choice by the Parties

(1) The rights and duties of the parties with respect to an issue in contract are determined by the local law of the state which, with respect to that issue, has the most significant relationship to the transaction and the parties under the principles stated in § 6.

(2) In the absence of an effective choice of law by the parties (see § 187), the contacts to be taken into account in applying the principles of § 6 to determine the law applicable to an issue include:

- (a) the place of contracting,
- (b) the place of negotiation of the contract,
- (c) the place of performance,
- (d) the location of the subject matter of the contract, and
- (e) the domicile, residence, nationality, place of incorporation and place of business of the parties.

These contacts are to be evaluated according to their relative importance with respect to the particular issue.

(3) If the place of negotiating the contract and the place of performance are in the same state, the local law of this state will usually be applied, except as otherwise provided in §§ 189–199 and 203.

Wisconsin has also applied the grouping-of-contacts analysis to marriage agreements. In *Knippel v. Marshall & Ilsley Bank (In re Estate of Knippel)*, 7 Wis. 2d 335, 96 N.W.2d 514 (1959), the court concluded that Wisconsin law should govern the validity and interpretation of a premarital agreement signed in Arizona before the parties married in that state. It appeared that the husband was at all times a Wisconsin resident, and that following the marriage and honeymoon, the wife left Arizona and came to Wisconsin to live, as both parties intended. Accordingly, Wisconsin was seen as having the most significant relationship to the parties and the performance of the agreement.

*Knippel* was decided before publication of the Restatement. However, it is a safe assumption that in future Wisconsin conflict-of-laws cases in which marriage agreements are silent on the choice of laws, the validity and interpretation of the agreement will be based on the analytical framework of Restatement section 188. See sections 13.38–.43, *infra*, for applicable rules when the law of a particular jurisdiction is chosen by agreement.



## C. Choice-of-laws Rules Relating to Property [§ 13.7]

### 1. In General [§ 13.8]

No recent Wisconsin cases have applied choice-of-laws principles to interests in property. The most recent statement on the subject was in *Knippel*, 7 Wis. 2d 335, in which the Wisconsin Supreme Court said

It is well established that regardless of the law of the place where a marriage is performed, the rights of the wife, in the absence of contract, with respect to her and her husband's personal property are governed by the law of the matrimonial domicile, and with respect to land, by the law of the situs.

*Id.* at 342. This position generally accords with the position taken in Restatement chapter 9 concerning choice-of-laws rules involving interests in movable and immovable property.

It is important to note that, as used in the following discussion and in the portions of the Restatement dealing with both immovable and movable property, the term *law* is defined as the *totality* of the law of the state where the immovable property is situated (or of the state that has the most significant relationship to the movable property or the parties), *including its choice-of-laws rules*, and not merely its “local law,” that is, its domestic substantive rules. Restatement § 222 cmt. e. Application of the totality of the law may produce a different result than applying the local substantive rule. See the example at section 13.10, *infra*.

### 2. Immovables [§ 13.9]

*Immovables* are defined as land and things that are so attached or otherwise related as to be regarded a part of it. Restatement ch. 9 introductory note to topic 2 (Immovables). The rule stated in the Restatement pertaining to immovables generally favors a legal characterization in accordance with the law of the situs. Section 234 of the Restatement provides,

§ 234. Effect of Marriage on an Interest in Land Later Acquired

(1) The effect of marriage upon an interest in land acquired by either of the spouses during coverture is determined by the law that would be applied by the courts of the situs.

(2) These courts would usually apply their own local law in determining such questions.

Despite this tilt in favor of the law of the situs in Restatement section 234, the Reporter's Note to that section indicates that in disputes between the spouses alone, the courts may attempt to characterize the real estate by looking to the nature of the property used to acquire it. Restatement § 234 reporter's note.

The rule of Restatement section 234 has not been universally followed, particularly when spouses have changed domicile, thus opening the door to use of tracing principles in determining the character of the property interest in real estate. W.S. McClanahan, *Community Property Law in the United States* § 13:2, at 569–70 (1982 & Supp. 1992); *see also Rustad v. Rustad*, 377 P.2d 414 (Wash. 1963); *Scott v. Currie*, 109 P.2d 526 (Wash. 1941). One commentator argues that the law of the situs should define real-property interests only for property acquired by gift or inheritance or as direct payment for services. Harold Marsh, Jr., *Marital Property in Conflict of Laws*, 100–03 (1952); *see also Trapp v. United States*, 177 F.2d 1 (10th Cir. 1949); *Hammonds v. Commissioner*, 106 F.2d 420 (10th Cir. 1939); *infra* §§ 13.44–.47.

The view that the law of the situs may occasionally yield to the law of the domicile is also found in Restatement chapter 9, introductory note to topic 2 (Immovables), which states, in part, as follows:

There will also be situations where the demands of certainty and the needs of a title recording system are not as pressing as are other demands. Thus, questions relating to the marital property interests of spouses, either upon divorce or at death, may be of greater concern to the state of domicile of the spouses than to the situs, and in such cases the situs courts might defer to the views of the domicile. That will particularly be so when the land is one item in an aggregate of things, both movable and immovable, which are situated in a number of states and which it is desirable to deal with as a unit.

A bias in favor of the law of the situs is also found in the provisions relating to contracts for the transfer of interests in land. Section 189 of the Restatement states,

The validity of a contract for the transfer of an interest in land and the rights created thereby are determined, in the absence of an effective choice of law by the parties, by the local law of the state where the land is situated unless, with respect to the particular issue, some other state has a more significant

relationship under the principles stated in § 6 to the transaction and the parties, in which event the local law of the other state will be applied.

The decision in *Mott v. Eddins*, 725 P.2d 761 (Ariz. Ct. App. 1986), illustrates the application of the rule. When a husband domiciled in California signed an agreement to purchase a residence in Arizona and later defaulted on the contract, the sellers sued both the husband and his wife for damages. The Arizona Court of Appeals concluded that Arizona had a more significant relationship to the transaction than California did, because the sellers were domiciled there, the real estate was located there, and the contract was executed and was to be performed there. Thus, Arizona law, which requires that both spouses must join in any transaction for the acquisition of real property, applied instead of California law, which allows a spouse acting alone to bind the community in a real estate purchase. Accordingly, the court directed that judgment be entered against the husband alone.

A similar result, albeit via a slightly different analysis, was achieved in *Wyss v. Albee*, 183 Wis. 2d 245, 515 N.W.2d 517 (Ct. App. 1994), *rev'd on other grounds*, 193 Wis. 2d 101, 532 N.W.2d 444 (1995), which involved a breach of contract for purchase of Wisconsin real estate from a Wisconsin resident by an Iowa partnership. One of the issues presented was whether the Wisconsin or the Iowa statute of frauds should apply to determine the validity of the land contract. Applying the choice-of-law considerations found in *Hunker*, 57 Wis. 2d at 598–99, the court concluded that the Wisconsin statute of frauds offered greater protection to Wisconsin residents and was the better choice of law. *Wyss*, 183 Wis. 2d at 263–64; *see also Triple Interest, Inc. v. Motel 6, Inc.*, 414 F. Supp. 589 (W.D. Wis. 1976).

### 3. Movables [§ 13.10]

*Movables*, defined as tangible or intangible things that are not immovables, are subject to different rules. Restatement ch. 9 introductory note to topic 3 (Movables). The introductory note states that in cases involving movables, the applicable law is generally the local law of the state that, with respect to the particular issue, has the most significant relationship to the parties, the thing, and the transaction. *Id.* This test is similar to the grouping-of-contacts rule for determining the choice of laws in contracts cases, found in Restatement section 188, a rule that has received judicial approval in Wisconsin. *See supra* § 13.6.

When marital property interests are involved, the state with the most significant relationship will generally be the state where the spouses were domiciled when the movable was acquired. A marital property interest acquired by either or both of the spouses while domiciled in one state is not affected by moving the property to a second state, regardless of whether the removal accompanies a change of domicile to the other state. Restatement section 258 contains the basic rule for movable personal property acquired during marriage:

§ 258. Interests in Movables Acquired during Marriage

(1) The interest of a spouse in a movable acquired by the other spouse during the marriage is determined by the local law of the state which, with respect to the particular issue, has the most significant relationship to the spouses and the movable under the principles stated in § 6.

(2) In the absence of an effective choice of law by the spouses, greater weight will usually be given to the state where the spouses were domiciled at the time the movable was acquired than to any other contact in determining the state of the applicable law.

It follows from this general rule that moving a spouse's personal property from one state to another does not change its legal character. Restatement section 259 confirms this view:

§ 259. Removal of Movables of Spouses to Another State

A [spousal] property interest in a chattel, or right embodied in a document, which has been acquired by either or both of the spouses, is not affected by the mere removal of the chattel or document to a second state, whether or not this removal is accompanied by a change of domicil to the other state on the part of one or both of the spouses. The interest, however, may be affected by dealings with the chattel or document in the second state.

Nor does the transmutation of the personal property into another form cause it to lose its character.

Restatement section 259 comment b states, in part the following:

When a chattel or document is taken into a second state and is there exchanged for some other movable or immovable, the spouses acquire the same interests therein as they had in the original chattel or document.

Some exceptions to these basic rules exist when interests of third parties such as creditors or transferees for value are involved; in those situations, the local law of the jurisdiction where the movable or immovable was located when the interest is claimed to have been

acquired will normally be applied. The application of choice-of-laws rules may be further muddled when transactions involve mixtures of property, contract, or tort law. In such cases, the laws of different states may be applied to different elements of the transaction.

Choice-of-laws questions in general, and those involving property law in particular, involve several levels of analysis. First, the issue must be characterized. For example, is it one of marital property or contract law? Marital property or tort? Marital property or the law of succession? Does it involve elements of more than one? Obviously, characterization can be a complicated process. It also can be used by the courts to control the result.

The following characterization cases illustrate the point. In *Polson v. Stewart*, 45 N.E. 737 (Mass. 1897), spouses, while domiciled in North Carolina, entered into a contract that involved mutual releases of any interest each had in the other's lands. After the wife died, the husband sought to assert an interest in the wife's Massachusetts lands in the courts of Massachusetts, claiming that his wife had lacked the power to make such a contract. Justice Holmes, writing for the majority, characterized the pivotal issue as the validity of the contract. Under the relevant Massachusetts choice-of-laws rule, the validity of such a contract was governed by the law of the place where it was made (North Carolina). Under North Carolina law, the wife had the capacity to make such a contract. Accordingly, the court held that the contract was valid and enforceable in Massachusetts. In dissent, Chief Justice Field characterized the contract as one for the conveyance of land. Under the applicable Massachusetts choice-of-laws rule, the validity of a conveyance was governed by the law of the situs of the land (i.e., Massachusetts). Under Massachusetts law, a husband and a wife could not convey lands directly to one another, and thus the contract for such a conveyance would have been void. 45 N.E. at 739–41 (Field, C.J., dissenting); see also *Jorgensen v. Crandell*, 277 N.W. 785 (Neb. 1938) (concerning postmarital agreement validly executed in California between California residents in which spouses gave up rights in each other's estates; holding that agreement was contract and not conveyance, thus barring wife from electing against husband's will in Nebraska with respect to devolution of Nebraska lands).

Another illustration of the difficulty inherent in characterizing the legal issue in a conflicts case is *Caruth v. Caruth*, 103 N.W. 103 (Iowa 1905). In *Caruth*, spouses executed a separation agreement in Illinois,

where the wife resided and where the agreement was valid. Under the agreement, the wife gave up all rights against the husband's estate. The husband subsequently moved to Iowa, where he died, leaving personal property. The wife sought her statutory share. Under Iowa statutes, inchoate rights were not property rights, and contracts conveying them were void. The Iowa Supreme Court characterized the issue before it as one of descent and distribution of a decedent's estate rather than one of contract. Because the decedent had died domiciled in Iowa and his property was located there, the Iowa court applied its law and held that the contract was void, permitting the widow to receive her statutory share. Had the court characterized the issue as one of contract, it is arguable that the relevant law would have been that of Illinois, where the contract was entered into and where it would have been valid, preventing the widow from collecting a statutory share.

These cases highlight the fact that spousal contracts, in contrast to most commercial contracts, can involve a variety of substantive rights and relationships leading to difficulty in characterizing the legal issue. Cases involving interests in land tend to focus the point. In *Kyle v. Kyle*, 128 So. 2d 427 (Fla. Dist. Ct. App. 1961), spouses executed a valid premarital agreement in Quebec while domiciled there. In the agreement, the wife specifically gave up any dower rights. Following the spouses' separation, the husband acquired real estate in Florida, which he later sought to convey to a Florida corporation that he controlled. When the wife refused to join in the deed to give up her inchoate dower rights, the husband asserted the contract and sought judgment declaring that the wife's dower had been relinquished. The court characterized the issue as one affecting title to Florida real estate rather than as one of contract. The applicable Florida choice-of-laws rule for title to real estate looked to the law of the situs of the real estate, which in this case was Florida. Florida law required the signatures of two witnesses for relinquishment of dower. Because the contract was only notarized and did not contain the requisite signatures of witnesses, it was not enforceable to bar the wife's dower interest. For a contrary and arguably sounder approach, see *Hill v. Hill*, 262 A.2d 661 (Del. Ch.), *aff'd*, 269 A.2d 212 (Del. 1970) (deeming premarital agreement, validly executed in Maryland, enforceable with respect to property in Delaware, despite differing formal requirements for such agreements under Delaware law).

Once an issue is characterized, the state whose substantive law is to be applied must be selected. In Wisconsin this is done by using the

choice-influencing considerations methodology, including grouping-of-contacts in contract cases. When the substantive law has been selected, the next step is to determine whether it includes only the substantive rules affecting the issue at bar or the other state's choice-of-laws rules as well. This is the doctrine of *renvoi*. If the other state's choice-of-laws rules (as well as its substantive rules) are adopted, the forum court may turn back to the substantive law of the forum. The following example illustrates the problem:

➤ **Example.** A married Wisconsin resident acquires farm real estate in Illinois in 1985 using property that is clearly deferred marital property under section 851.055. She dies a resident of Wisconsin in 1986, survived by a husband and two adult children, all domiciled in Wisconsin. Her will substantially disinherits her husband. Under the Wisconsin deferred marital property election statute, Wis. Stat. § 861.02, the husband may elect up to one-half of the deferred marital property; under the Illinois statute governing renunciation of the will by the surviving spouse, 755 Ill. Comp. Stat. Ann. 5/2-8(a) (current through P.A. 96-890 of the 2010 Reg. Sess.), the husband is entitled to one-third of the entire estate of the decedent. In Illinois ancillary probate proceedings, the husband asks the court to apply the Wisconsin deferred marital property election statute. One of the adult children objects, insisting that the husband is entitled to no more than the one-third share under Illinois law.

If Illinois has a strong *lex loci* conflict-of-laws rule for real estate, the local probate court would simply apply its own substantive law (i.e., the Illinois renunciation-of-will statute) to determine the outcome. Assume, however, that the Illinois probate court, applying relevant Illinois choice-of-laws principles, decides that because the spouses (and the children) resided in Wisconsin and the wife died there, and because Wisconsin's deferred marital property statute better evinces its policy of protecting surviving spouses, it will apply Wisconsin law. Assume further that Wisconsin has a strong *lex loci* conflict-of-laws rule for real estate, and that Wisconsin courts would apply Illinois law if the matter were before them for adjudication, with the result that the surviving husband would receive only a one-third interest in the real estate. The question is thus whether the Illinois court will apply only the Wisconsin substantive rule (i.e., the deferred marital property election statute) or its choice-of-laws rule as well. If it applies only the Wisconsin substantive rule, the Illinois court would give the husband one-half of the Illinois farm; if the court applies Wisconsin's choice-of-laws rule as well, it might end up using

Illinois substantive law (i.e., the Illinois renunciation-of-will statute), thus giving the husband only a one-third interest in the farm. *See* Marsh, *supra* § 13.9, at 69–75.

➤ **Note.** It is not clear that the Wisconsin court would unquestioningly apply the law of Illinois to the real estate located there under the rule stated in *Knippel*, 7 Wis. 2d 335, and Restatement section 234 in light of *Heath*, discussed in section 13.5, *supra*, and its progeny.

#### **D. Conceptual Problems of Marital Property (i.e., Community Property) Versus Common Law Forms of Ownership [§ 13.11]**

Most of the conflict-of-laws questions generated by Wisconsin's marital property regime will probably involve transfers of a married person's property from one state to another, whether or not accompanied by a change of domicile. Questions will arise as long as Wisconsin laws governing the ownership of property acquired by married persons differ substantially from those of states with common law property systems—and this includes all of Wisconsin's neighboring states—and differ to some extent from those of other community property states.

Under a community property regime like Wisconsin's marital property system, if either spouse acquires community property (marital property under the Act) during the marriage, each spouse has a present, vested, and equal ownership interest in it, regardless of who has title or possession. Under a community property system, separate property (individual property under the Act) refers generally to property owned before marriage, property acquired by a spouse after marriage through gift or inheritance, or property traceable to those sources. The nonowner spouse acquires no interest in this civil law separate property during the marriage or at death.

Under the common law system, there is no element of shared ownership for property acquired in the name of one spouse during marriage. Ownership rights are determined solely by title or possession. Property titled in the name of, or exclusively possessed by, either spouse is the solely owned property of that spouse. Common law solely owned property has also been referred to as *separate property*, although it



frequently is burdened with legal rights favoring the other spouse (e.g., dower, curtesy, or statutory rights at divorce or death). These rights in favor of the other spouse are unknown to civil law separate property in all the community property states.

The right of a surviving spouse in the common law solely owned property of the decedent spouse typically consists of a statutory elective share in lieu of common law dower or curtesy or a right to elect against the provisions made in the decedent's will. In contrast, a surviving spouse under a community property system normally has no statutory or other rights to exercise against the civil law separate property of the deceased spouse. The difference arises because the classification rules and presumptions of a community property system tend to favor creation of community property in the hands of spouses and because of the vested one-half interest that automatically arises in each spouse upon creation of community property.

A major historic problem in choice-of-laws cases involving the property rights of married persons arose because of the semantic difficulty experienced by courts in community property jurisdictions in recognizing the substantial differences between the legal characteristics of common law solely owned separate property and the legal characteristics of civil law separate property under a community property system. Marsh, *supra* § 13.9, at 224. Similarly, the courts in common law jurisdictions have had equally great semantic difficulty in dealing with community property, a form of ownership unknown to the common law. Failing to recognize that significant differences exist in the legal characteristics of the forms of ownership being compared, courts in both kinds of jurisdictions have often incorrectly equated common law solely owned property to civil law separate property or have equated community property to some indigenous form of common law ownership such as tenancy in common or tenancy by the entireties. William Q. de Funiak & Michael J. Vaughn, *Principles of Community Property* § 3 (2d ed. 1971); McClanahan, *supra* § 13.9, at §§ 1:9, 1:13, 13:3–13:6; *see, e.g., Estate of Hanau v. Hanau*, 730 S.W.2d 663 (Tex. 1987) (discussed in section 13.15, *infra*). This has sometimes been referred to as the *play-on-words* approach.

The potential inequities of this approach are widely recognized. In community property states, several solutions have been advanced for dealing with property rights upon termination of a marriage by dissolution or death following a change of domicile. William Reppy and

Symeon Symeonides address this problem and possible solutions in the context of a proposed marital property statute. William Reppy, *Viewpoint: Louisiana's Proposed "Hybrid" Quasi-Community Property Statute Could Cause Unfairness*, Community Prop. J., Oct. 1986, at 1; Symeon Symeonides, *In Search of New Choice-of-Law Solutions to Some Marital Property Problems of Migrant Spouses: A Response to the Critics*, Community Prop. J., Oct. 1986, at 11.

Both Reppy and Symeonides discuss a proposed Louisiana statute governing successions in marital property. Both authors deal with the theoretical and practical difficulties of protecting spousal property rights either at dissolution or at death after a change of domicile from a common law jurisdiction to a community property state. Reppy discusses the principal solutions. One alternative is the *borrowed-law approach*, in which the forum court simply applies the property-division or spousal-election law of the former state of domicile to property that was acquired while the spouses lived in the former state. If the spouses have lived in only one other state, and if the property acquired there is readily identifiable, this approach can be a fair solution that accords with the spouses' expectations. It can pose obvious difficulties, however, if the spouses have been domiciled in several states before residing in the state in which their marriage ends. It can also be problematic if the property acquired by the spouses in the former and the current states of domicile is hopelessly commingled. Finally, it requires the courts of the forum state to educate themselves about the applicable laws of another jurisdiction. See Reppy, *supra* § 13.11, at 3–4.

A more generally favored solution in community property states has been to legislatively apply quasi-community property principles to the property acquired by the spouses while living in other jurisdictions. This was the choice made in Wisconsin. See *supra* §§ 2.222, 2.226 (general discussion of the quasi-community property principles adopted in Wisconsin as part of the Act). Under the quasi-community property approach, a domiciliary community property state analyzes assets acquired in other jurisdictions to determine how they would be classified under its own laws when the marriage terminates and treats the classification of the assets consistently with its own law.

Symeonides defends the Louisiana statute, which combines the traditional quasi-community property approach and the borrowed-law approach. Symeonides explains why the drafters believed that the statute would provide the fairest result under a variety of factual scenarios that

might occur following a change of domicile. On the other hand, Reppy concludes that the “pure” quasi-community property approach produces the fairest result under most circumstances and argues that the proposed Louisiana statute should follow that route.

### **III. Application of Choice-of-laws Principles [§ 13.12]**

#### **A. Common Law Solely Owned Property Brought to Wisconsin Upon Change of Domicile to Wisconsin [§ 13.13]**

##### **1. In General [§ 13.14]**

As a result of the Marital Property Act, choice-of-laws questions will arise more frequently upon death or dissolution of a marriage, or when a creditor’s claim is asserted against movable common law property brought into Wisconsin or against assets acquired with such property. When the Act does not supply a solution, it is helpful to analyze the experience of other community property states in predicting how Wisconsin courts will deal with these matters.

A number of important early cases concerning movables brought from a common law state to a community property state in the course of a change of domicile are discussed by McClanahan, *supra* § 13.9, § 3:7. The general principle emerging from these cases is that property acquired in and brought from the common law state, and subsequently reinvested in personal property or real estate in the new state of domicile, will not lose its legal characteristics. *Id.*; *see also supra* §§ 13.7–10. By the same token, property acquired after the change of domicile (and not traceable to an earlier acquisition in the common law state) will be characterized under the community property laws of the new domicile. *Id.*

The importance of this choice-of-laws rule for persons moving into Wisconsin is that, absent any specific statutory provision to the contrary, Wisconsin courts should continue to recognize the common law characteristics of property previously acquired in a common law jurisdiction, including property subsequently acquired in Wisconsin that is traceable to that property. Such treatment is consistent with section 766.31(8), which provides that except as provided otherwise in chapter

766, predetermination date property classifications and ownership rights are not altered by the Act. And, it should be recalled, the determination date for persons moving into Wisconsin after the effective date of the Act is the date that both spouses are domiciled here. Wis. Stat. § 766.01(5)(b).

This is not to imply that the Act has no effect on common law solely owned property brought into Wisconsin. It has an effect in a variety of ways. The presumption in section 766.31(2) that all property of spouses is marital property applies, and the spouse contending that the property has a different classification must overcome that presumption. Similarly, under the mixed-property reclassification rule of section 766.63(1), a spouse who contends that part of the mixed property is not marital property must be able to trace the nonmarital property to demonstrate that fact. The rule of section 766.63(2) that marital property can be created through the substantial efforts of a spouse that are not adequately compensated also applies to predetermination date “other” property as well as individual property, and this, too, affects the characterization process. Additionally, the income rule of section 766.31(4), which classifies the income “attributable to property of a spouse during marriage” as marital property, applies to the property of new residents, unless a spouse executes a unilateral statement under section 766.59. *See* Unif. Marital Property Act § 4 cmt., 9A U.L.A. 118 (1998). (The Uniform Marital Property Act [hereinafter UMPA] is reprinted in appendix A, *infra*.) And the augmented deferred marital property election in section 861.02 applies in the event of death while the spouses are domiciled in Wisconsin, aided by a presumption that the property of the spouses is deferred marital property if the presumption of marital property in section 766.31(2) is rebutted.

The crucial points for determining the legal characteristics of property are at death, dissolution of the marriage, or assertion of a creditor’s claim. These are examined separately below.

## **2. Death of a Spouse [§ 13.15]**

Sections 861.01, 857.01, 858.01, and 859.18 contemplate an early examination and classification of a deceased spouse’s assets and obligations under chapter 766. If a surviving spouse wants to exercise elective rights under section 861.02, a determination of whether the decedent or the surviving spouse owned deferred marital property is also

necessary. *Deferred marital property* is defined by section 851.055 as all property that is not classified by chapter 766; that was acquired while the spouses were married; and that would have been classified as marital property if the property had been acquired when chapter 766 applied. The probate and nonprobate deferred marital property assets of both spouses are included in the augmented deferred marital property estate under sections 861.03 and 861.04. The augmented deferred marital property estate is subject to various exclusions and adjustments described in section 861.05. This augmented deferred marital property estate is subject to a surviving spouse's right of election under section 861.02. The surviving spouse may elect no more than 50% of the augmented deferred marital property estate, subject to satisfaction rules contained in sections 861.06, 861.07, and 861.11. *See supra* §§ 12.148–162.

The deferred marital property election statute represents a legislative effort to eliminate inequities that might occur when spouses move to Wisconsin after the determination date with common law solely owned property. Because the elective-share provisions of prior law (i.e., Wis. Stat. §§ 861.03–.15 (1983–84)) were repealed by the Act, the election also reaches predetermination date property owned by married persons who resided in Wisconsin before the effective date of the Act. To better understand the need for such a statute, a review of the judicial treatment of common law solely owned movables brought into a community property jurisdiction is helpful.

In other community property jurisdictions, early cases with the following choice-of-laws scenario proved troublesome. The spouses moved into the community property jurisdiction with common law solely owned assets. The titled spouse then died, leaving a will disinheriting the other spouse. In response to a challenge to this arrangement, the court in the community property jurisdiction might determine that the solely owned assets (or separate property) acquired in the common law jurisdiction were the same as civil law separate property in the community property state. Because the community property jurisdiction provided the surviving spouse with no rights, elective or otherwise, in civil law separate property, the decedent spouse was free to dispose of the solely owned assets as he or she saw fit, even to the extent of disinheriting the surviving spouse. What happened in this process, of course, was that judicial equation of common law solely owned property with civil law separate property under a community property regime stripped away all the common law spousal protections such as dower, curtesy, and statutory elections, that were legal characteristics of the

solely owned property in the state of acquisition. See *In re Estate of Higgins*, 4 P. 389 (Cal. 1884); McClanahan, *supra* § 13.9, §§ 13:4–13:6.

The problems with this play-on-words approach to dealing with property acquired in a common law jurisdiction and brought to a community property jurisdiction are illustrated by the Texas Supreme Court's decision in *Estate of Hanau v. Hanau*, 730 S.W.2d 663 (Tex. 1987). The spouses were married in Illinois and resided there for five years before moving to Texas, where they resided until the husband's death. Each spouse had accumulated substantial amounts of solely owned property before marriage and made efforts to keep this property segregated. The husband also acquired significant assets during the marriage. After moving to Texas, the husband, who had children by a prior marriage, prepared a will leaving his separate property to these children and his community property interest to his wife.

Following the husband's death, the wife and the husband's children disputed the proper allocation of the assets under the will. The wife contended that the court should extend the Texas quasi-community property rule at divorce, found in Texas Family Code Annotated section 3.63(b) (Vernon 1993) and amplified by *Cameron v. Cameron*, 641 S.W.2d 210 (Tex. 1982), to situations involving dissolution of a marriage by death. (Section 3.63(b) was repealed in 1997. The comparable provision of the current statutes is Texas Family Code section 7.002 (current through the end of the 2009 Regular and First Called Session of the 81st Legislature).) If the quasi-community property rule were applied, the substantial property interests acquired during the five years when the spouses resided in Illinois would be treated as if they were community property, and the wife would receive this property under the decedent's will.

The Texas Supreme Court declined to judicially extend the quasi-community property rule (which permits equitable division at divorce of property acquired in another jurisdiction that would have been community property if acquired in Texas) to situations involving the death of a spouse. The court reiterated its long-standing general rule that "property which is separate property in the state of the matrimonial domicile at the time of its acquisition will not be treated for probate purposes as though acquired in Texas." *Hanau*, 730 S.W.2d at 665. Thus the court equated solely owned assets acquired in a common law jurisdiction (Illinois) with Texas civil law separate property. This had the effect of depriving the surviving spouse of any protections that would

have attached to the solely owned property if the spouses had remained domiciled in Illinois, such as the wife's right to elect a statutory share.

In response to the inequity of investing common law solely owned assets with the attributes of civil law separate property, several community property states have adopted statutes of succession, often referred to as quasi-community property statutes, that apply at the death of a spouse. California's statute was first, and provided that upon the death of a spouse, assets acquired during the marriage while the spouses were domiciled elsewhere that would not have been civil law separate property if the spouses had been domiciled in California, belong one-half to the decedent spouse and one-half to the surviving spouse, subject to the debts of the decedent. Cal. Prob. Code § 201.5 (West 1984); *see also* Idaho Code §§ 15-2-201 to 15-2-203 (current through (2010) Chs. 1-223 and HJR's 4, 5, and 7 that are effective on or before March 31, 2010). The California quasi-community property statute was revised effective January 1, 1985 and again effective July 1, 1991. Although it remains essentially the same in concept, the reach of the statute has been altered somewhat. *See supra* § 2.222.

Sections 851.055 and 861.018-.11 derive from these quasi-community property statutes. *See* UMPA § 18 cmt.; *see also* Wis. Stat. § 766.77(1) (before its repeal by 1985 Wisconsin Act 37 [hereinafter 1985 Trailer Bill]); *supra* §§ 2.222-2.238. The importance of these statutory provisions is that they apply the principles of the Act to all assets owned at the time of death by spouses domiciled in Wisconsin that were acquired during marriage and before the spouses' determination date and that would have been marital property if they had been acquired after the determination date. These statutes apply to assets acquired during marriage in common law and community property jurisdictions alike. If a surviving spouse wants to make an election under the statutes, a Wisconsin personal representative must investigate the time, manner, and sources of acquisition of the decedent's and the surviving spouse's assets. If all or part of the assets are shown to have been acquired before the marriage, through gift or inheritance, through distributions from a trust created by a third party, or with the reinvested proceeds of any of the above, they are not subject to the surviving spouse's right of election under the statutes. However, if an investigation shows that the assets would have been marital property under the Act, then they are included in the augmented deferred marital property estate and are subject to the elective rights of section 861.02 regardless of whether they are probate or nonprobate assets. Those probate deferred marital property assets not

required for satisfaction of the augmented deferred marital property elective share continue to be subject to disposition by the deceased spouse's will or under the intestate succession statute. Those nonprobate deferred marital property assets remaining after the satisfaction of the augmented deferred marital property elective share would remain the property of the original transferees from or appointees of the decedent and any donees of those transferees.

### **3. Divorce [§ 13.16]**

Before its repeal by the 1985 Trailer Bill, section 766.75(1) contained a statutory deferred marital property concept that applied at divorce. This statute provided that all property owned at the time of dissolution of the marriage by either or both spouses that was acquired during marriage and before the determination date, and that would have been marital property under the Act if acquired after the determination date, was to be treated as if it were marital property. This provision was repealed by the 1985 Trailer Bill because of concern that it might be interpreted as a constraint on a divorce court in arriving at an equitable division of property under section 767.61 (formerly section 767.255).

A number of community property states have adopted quasi-community property statutes that operate like former section 766.75(1) in the event of divorce. *See* Ariz. Rev. Stat. Ann. § 25-318 (current through legislation effective February 9, 2010 of the Sixth Special Session, and legislation effective April 16, 2010 of the Second Regular Session of the Forty-Ninth Legislature (2010)); Cal. Fam. Code § 125 (current with all 2009 Reg. Sess. Laws; all 2009-2010 1st through 5th, 7th, and 8th Ex. Sess. Laws; urgency legislation through Ch. 17 of the 2010 Reg. Sess.; and propositions on the 6/8/2010 ballot); Tex. Fam. Code Ann. § 7.002 (current through the end of the 2009 Regular and First Called Session of the 81st Legislature). Once again, the statutory provision is a response to the historic tendency of courts in community property jurisdictions to confuse common law solely owned property brought into a state with civil law separate property and thus to exclude it from division at divorce.

The issue of improper judicial characterization typically has arisen when a community property state's divorce statute equally divides the *community* property of the spouses but does not authorize dividing the *separate* property owned by either spouse. If the period of domicile in



the community property state before the divorce was short, the amount of community property accumulated by the spouses is likely to be small compared to the amount of common law solely owned property. If the courts equated the common law solely owned property with separate civil law property, then inequitable results were likely. *See Latterner v. Latterner*, 8 P.2d 870 (Cal. Ct. App. 1932); William A. Reppy, Jr. & Cynthia A. Samuel, *Community Property in the United States* 359–69 (2d ed. 1982); McClanahan, *supra* § 13.9, §§ 13:4–13:6.

Where, however, divorce courts in community property jurisdictions have eluded the semantic trap of equating common law “separate” property with civil law separate property (see discussion at section 13.15, *supra*), they have reached fair results by characterizing the property as it would be characterized under the laws of the state in which the spouses were domiciled when the property was acquired and then allocating the property according to the laws of that state. *See Burton v. Burton*, 531 P.2d 204 (Ariz. Ct. App. 1975); *Rau v. Rau*, 432 P.2d 910 (Ariz. Ct. App. 1967); *Berle v. Berle*, 546 P.2d 407 (Idaho 1976); *Gilbert v. Gilbert*, 442 So. 2d 1330 (La. Ct. App. 1984); *Braddock v. Braddock*, 542 P.2d 1060 (Nev. 1975); *Hughes v. Hughes*, 573 P.2d 1194 (N.M. 1978); *Cameron v. Cameron*, 641 S.W.2d 210 (Tex. 1982).

Divorce inequities like those described above are not likely to arise in Wisconsin. Section 767.61 is a broad-gauge statute providing for an equitable division of all property of the spouses upon termination of the marriage. It calls on the court to “divide the property of the parties” and directs that “title to the property of the parties be transferred as necessary, in accordance with the division of property set forth in the judgment.” Wis. Stat. § 767.61(1), (5)(a). The only significant exceptions are for property acquired by gift or inheritance or with funds acquired by gift or inheritance, but even that exception does not apply if refusing to divide the property would create a hardship for the other party or the children of the marriage. The breadth and scope of section 767.61 make it reasonable to expect that the courts will throw both marital property and property other than marital property (including common law solely owned property acquired in another state) into the pot for equitable division. Only inherited or gifted property will ordinarily be excluded from the asset division. *See supra*, § 11.13–.15.

#### 4. Assertion of Creditors' Claims [§ 13.17]

Interesting choice-of-laws problems involving the enforcement of a creditor's claim often follow a change of domicile. Courts have tended to apply the law of the place where the debt was incurred both to the categorization of the debt and to the determination of which assets were available for its satisfaction if the spouses resided in that jurisdiction when the debt arose. In Wisconsin, this appears to be mandated by statute. Section 766.55(3) states that chapter 766 does not alter the relationship between the spouses and their creditors with respect to obligations in existence on the determination date. The determination date for spouses moving into Wisconsin after the effective date of the Act is the date they both are domiciled in Wisconsin. Wis. Stat. § 766.01(5)(b). If the obligation were incurred in the state of former domicile, its laws will presumably continue to apply.

*Pacific Gamble Robinson Co. v. Lapp*, 622 P.2d 850 (Wash. 1980), illustrates the choice-of-laws problems involving creditors' claims. *Lapp* involved a creditor's action in Washington to recover on a promissory note executed in Colorado by the husband alone when the spouses were domiciled in Colorado. Applying the grouping-of-contacts analysis of Restatement section 188 to the transaction, including the expectations of the parties, the court ruled that Colorado's interest was more significant than Washington's and it therefore applied Colorado law. The law of Colorado, a common law state, subjected all the spouses' property to the debt except for the wife's Colorado "separate property," that is, her solely owned property including her earnings. Accordingly, the court concluded that Colorado law also defined the boundaries of what was recoverable in Washington—in effect, the husband's wages and earnings. This was true despite the fact that under Washington community property law only the husband's civil law separate property (and not his wages) would have been reachable to satisfy a debt for the benefit of his separate property, and only the wages and earnings of *both* spouses (plus all other community property) would have been reachable for a debt benefiting the community.

The dissent in *Lapp* said that Washington law should determine the source and classification of funds used to satisfy the obligation, while Colorado law should determine the validity of the obligation in the first instance. Under this analysis, the debt would have been classified as a separate debt of the husband, with the community property (i.e., the wages) of both spouses relieved from its satisfaction. 622 P.2d at 857–

61 (Horowitz, J., dissenting). Presumably the husband had no civil law separate property for the creditor to reach.

Aided by the statutory directive of section 766.55(3) that chapter 766 does not alter the relationship between spouses and their creditors for predetermination date obligations, it is likely that if the Wisconsin Supreme Court were confronted with the facts of the *Lapp* case, it would determine that the former state of domicile had the most significant contacts with the transaction and would apply its laws. This view was adopted in *In re Sweitzer*, 111 B.R. 792 (Bankr. W.D. Wis. 1990) (citing 3 Keith A. Christiansen et al., *Marital Property Law in Wisconsin* § 13.10c, at 13-23, 13-24 (State Bar of Wisconsin CLE Books 2d ed. 1986 & Supp. 1988)). The husband incurred a debt while the spouses were Ohio residents. The creditor reduced the debt to judgment against the husband while the spouses were still Ohio residents. Shortly thereafter the spouses moved their domicile to Wisconsin; subsequently, the wife alone filed a petition for bankruptcy. Later, the creditor sought to garnish the husband's wages (including the wife's marital property interest therein) to satisfy its judgment. The bankruptcy court declined to issue an injunction barring the creditor from garnishing the husband's wages, holding that Ohio law applied to determine which assets were available for recovery. Based on its analysis of section 766.55(3), the court held that all the husband's income was available to the creditor just as it would have been had the spouses remained in Ohio and regardless of any marital property rights that might have otherwise arisen under Wisconsin's marital property statutes. Because the husband's earnings would not be treated as community property under Ohio law, the wife's discharge in bankruptcy did not protect his earnings even though it ordinarily would protect community property acquired after the discharge. See 11 U.S.C. § 524(a)(3); see also *supra* § 6.108.

The discussion up to this point has involved the situation in which the spouses resided in the jurisdiction where the debt was incurred. The result is likely to be different, however, when spouses reside in one state and incur a debt in another. Under these circumstances, the courts have tended to emphasize the importance of the state of residence in reaching a choice-of-laws decision. For example, in *Potlatch No. 1 Federal Credit Union v. Kennedy*, 459 P.2d 32 (Wash. 1969), the husband, a resident of Washington, co-signed a note for a loan an Idaho lender made to his brother. Under the significant-relationship and grouping-of-contacts analyses, the court applied Washington law and held that the obligation did not benefit the community and, further, that the

community property of the co-signer was not available to satisfy such an obligation. A similar result was reached in *Colorado National Bank v. Merlino*, 668 P.2d 1304 (Wash. Ct. App. 1983), in which the husband and wife resided in Washington, and the husband alone contracted to purchase real estate in Colorado. By Washington statute, no community obligation arose without the signatures of both spouses on the real estate purchase contract. Thus, under Washington law, the husband's obligation was characterized as his separate debt, which was enforceable only against his separate property. The community property assets of the spouses (including their earnings) were not subject to satisfaction of the debt.

A similar result on a reverse fact situation was involved in *Lorenz-Auxier Financial Group, Inc. v. Bidewell*, 772 P.2d 41 (Ariz. Ct. App. 1989). The spouses were domiciled in Oregon, a non-community property state, and the husband entered into equipment leases in Arizona, a community property state. The equipment leases contained a choice-of-laws provision indicating that Arizona law was to govern interpretation of the agreements. Subsequently, the husband defaulted on the leases. The equipment lessor then commenced an action against both the husband and the wife (who had not signed the equipment leases), contending that because the lease agreement contained an Arizona choice-of-laws provision, Arizona's community property debt-satisfaction rules should be applied. Under Arizona law, debt incurred by one spouse while acting for the benefit of the marital community is a community obligation regardless of whether the other spouse approves it. Debts incurred during marriage are presumed to be community obligations. If these rules had been applied to the defendant spouses, any of the wife's assets that would have been community property under Arizona law (but not under Oregon law) would have been reachable by the equipment lessor. The Arizona Court of Appeals concluded, however, that the law of Oregon, a non-community property state, applied to the transaction, because the spouses at all relevant times resided in that state. Under Oregon law, only the husband's separate property could be reached to satisfy a debt that he alone incurred. Accordingly, the court concluded that under Oregon law, the wife's property was not susceptible to judgment on the debt. A key element in the court's holding is the fact that the wife had never signed the equipment leases and thus was not bound by the choice-of-laws provision in the lease agreements.

Arizona also refused to allow recovery against a California couple's community property in a situation in which the husband alone entered into a personal guaranty of a lease of Arizona real estate to a business entity in which he was involved. Arizona was the place of the execution, negotiation, and performance of the guaranty and the site of the leasehold interest. Arizona has a statutory rule (Ariz. Rev. Stat. § 25-214) requiring both spouses to join in a guaranty of a third party's obligation to bind their community property, whereas California does not have such a rule. The obligee on the guaranty brought suit in Arizona seeking to recover from all the couple's community property through application of California law. Applying Restatement sections 6 and 194, the Arizona Court of Appeals concluded that Arizona had the most significant relationship to the transaction, and ruled that it would not mechanistically follow its holding in *Bidewell* that the law of the marital domicile (here California) controls. The key to understanding this case is that the California wife did not join in the leasehold guaranty, and the court was reluctant to undermine the statutory protections afforded by Arizona law that require both spouses to join in a guaranty of a third party's obligation. Thus, the more protective policies of Arizona were applied. Said differently, having determined that Arizona had the most significant relationship, the husband's unilateral guaranty was simply insufficient under Arizona law to bind the California couple's community property. *Phoenix Arbor Plaza, Ltd. v. Dauderman*, 785 P.2d 1215 (Ariz. Ct. App. 1989).

For an analysis of the application of the significant-relationship test in multijurisdictional creditors' rights cases, see Scott Fehrman, *Conflict of Laws: The Availability of Community Property to Satisfy a Judgment*, Community Prop. J., Oct. 1988, at 28. The author advocates applying the significant-relationship test sequentially, first to determine the validity and effect of the contract and then to determine the property available for contractual damage recovery. When a contract is made or performed in one state and enforcement is sought in a second state where the spouses are domiciled, the laws of the two different states may have a significant relationship to different elements of the transaction.

The author concludes that if the contracting spouse alone has the capacity to enter into a contract binding on the community under the law of the significant-relationship state (where the contract was made and performed) but not under the law of the domiciliary state, the law of the domiciliary state should determine the availability of property for recovery to protect the noncontracting spouse. *Id.* at 36. Conversely, if

the contracting spouse alone lacks capacity to enter into a contract binding on the community in the significant-relationship state, but has such capacity in the domiciliary state, the law of the significant-relationship state should determine the rights of recovery. *Id.* Under this analysis, *Kennedy*, *Merlino*, *Bidewell* and *Dauderman* were correctly decided, but *Lapp* was not.

Equally complex questions arise in determining when a transmutation in the form of ownership of assets resulting from a change in domicile cuts off the rights of creditors. One decision analyzing the effects of the form of ownership of property on the rights of creditors is *Bricks Unlimited, Inc. v. Agee*, 672 F.2d 1255 (5th Cir. 1982). In that case, the husband had incurred a community debt while the spouses resided in Louisiana. The spouses then moved to Mississippi, a common law state, and bought a house there as joint tenants. The source of funds used to purchase the real estate was not indicated. The Louisiana creditor sued and obtained a judgment for the debt. The spouses sold their jointly owned residence in Mississippi, accepting a note payable to both of them as part of the purchase price. Next, they moved back to Louisiana and jointly assigned the note to a Louisiana bank as collateral for another loan.

The judgment creditor attempted to garnish the maker of the purchase money note. The court determined that the Louisiana bank was a holder in due course and had a priority right to satisfaction out of the proceeds of the purchase money note. As to the balance of the note, the court held that the Louisiana judgment creditor could not reach the wife's one-half of the net proceeds. That interest, attributable to a common law joint ownership in real estate, was the wife's separate property. Under Louisiana law, a spouse's separate property cannot be reached to satisfy a community debt incurred by the other spouse. Apparently, the creditor in this case introduced no evidence to prove that the Mississippi residence was acquired with community property. If this key fact had been proved, it would have squarely raised the legal question of whether spouses may intentionally transmute community property into some other form of ownership to avoid the reach of creditors.

Under the Act, the result in *Agee* might be different. Assume that the defendant spouses moved out of and then back into Wisconsin and acquired their intermediate residence in Illinois. Assume further that the Illinois residence was acquired in joint tenancy with a down payment consisting of Wisconsin marital property. Under these circumstances, a

Wisconsin court might find that, despite Restatement section 234, the court would not permit the entire proceeds of sale of the Illinois real estate to be recharacterized as common law joint tenancy property. Without recharacterization, most of the proceeds—including the wife's share—would remain marital property and would be available to satisfy a family-purpose debt incurred during the earlier period of residence in Wisconsin. Alternatively, a Wisconsin court might rule that investing marital property in an Illinois joint tenancy effectively transmuted the marital property, thus limiting the creditor's recovery to the one-half of the joint tenancy owned by the spouse who incurred the obligation.

On the other hand, if the Illinois real estate were acquired with the individual property of one or both spouses, or with predetermination date Wisconsin solely owned or joint tenancy property, a Wisconsin court would probably reach the same conclusion as the *Agee* court.

In an apparent effort to address the problems inherent in *Agee*-type situations, the 1985 Trailer Bill adopted a statutory section intended for the ears of courts in other jurisdictions that care to listen. Section 766.55(7) states that property available under chapter 766 to satisfy an obligation of a spouse is available regardless of whether the property is located in this state. The 1985 Trailer Bill Note to section 766.55(7) acknowledges that recognition of the provision may be subject to the laws of other jurisdictions but states that it may aid creditors in attempting to satisfy obligations covered by chapter 766 in other jurisdictions. Wis. Stat. Ann. § 766.55 Legis. Council Notes—1985 Act 37, §§ 90 to 98 (West 2009). Clearly, physically removing marital property movables acquired while the spouses were domiciled in Wisconsin to a common law state (and perhaps titling them in the name of the nonincurring spouse alone) should not, under the principles of Restatement sections 258 and 259, transmute the movables and defeat the recovery rights of creditors. In these situations, section 766.55(7) suggests the result that the courts of the new domiciliary jurisdiction should reach under well-established choice-of-laws principles.

More difficult is the situation in which a creditor seeks to reach the future earnings of a spouse domiciled in a common law jurisdiction to satisfy a family-purpose obligation incurred by the other spouse while the spouses were domiciled in Wisconsin. *See supra* ch. 5. The analysis in *Lapp* supports the view that the nonincurring wage-earning spouse's establishment of a new domicile will not defeat the right of the other spouse's creditor to reach 100% of the wage earner's earnings in

satisfaction of the obligation, despite the fact that the income is now common law solely owned property. On the other hand, it is equally possible that a court in the new state of domicile might deny recovery because (1) the wage earner is not personally liable for the debt, (2) a family-purpose obligation can be satisfied only from all marital property (or from all other property of the *incurring* spouse), and (3) the wages of the nonincurring spouse are no longer marital property. Section 766.55(7) may at least be considered by the courts of the new domiciliary jurisdiction in reaching a decision on the appropriate substantive law to apply in determining what property is available to satisfy the debt.

1987 Wisconsin Act 393 [hereinafter 1988 Trailer Bill] further amended section 766.55(7) to clarify that the provision on nonimpairment of creditors' rights applies not only when marital property assets are removed to another jurisdiction but also when the marital property laws cease to apply because one or both spouses are no longer domiciled in Wisconsin. The apparent intent of this provision was to buttress the rights of a creditor in pursuing the future earnings of a nonincurring spouse who becomes domiciled in another state when the underlying debt is a family-purpose obligation incurred by the other spouse while both spouses were domiciled in Wisconsin. As noted above, it is not clear that the courts in other jurisdictions will be willing to give long-arm effect to Wisconsin's statutory rules regarding the satisfaction of obligations.

The legislature amplified on the subject of nonimpairment of creditors' rights by enacting section 766.03(6) as part of 1991 Wisconsin Act 301 [hereinafter 1992 Trailer Bill]. Unlike section 766.55(7), which applies to obligations incurred by a spouse while both spouses are domiciled in Wisconsin, section 766.03(6) expressly applies to situations in which an obligation is incurred or arises at a time when one or both spouses are domiciled in another state and the Act therefore does not apply. Section 766.03(6) provides that chapter 766 does not affect the property available to satisfy an obligation incurred by a spouse if the obligation arises at a time when one or both spouses are not domiciled in Wisconsin or arises from an act or omission occurring when one or both spouses are not domiciled in Wisconsin. The Legislative Council Notes to this provision state, in part, the following:



The substance of this provision is implicit under ch. 766. It is made explicit because its absence, in light of the detailed provisions under s. 766.55 on what property is available to satisfy obligations, has raised questions.

Wis. Stat. Ann. § 766.03 Legis. Council Notes—1991 Act 301, § 11 (West 2009).

It seems obvious that chapter 766 does not affect the property available to satisfy an obligation incurred or arising at a time when the Act does not apply because one or both spouses are domiciled elsewhere. The Legislative Council Notes to section 766.03(6) view that subsection as consistent with other provisions in section 766.55 that leave creditors where they otherwise would have been in the absence of the Act. *See* Wis. Stat. Ann. § 766.03 Legis. Council Notes—1991 Act 301, § 11 (West 2009). That is, it prevents creditors from using the debt-satisfaction provisions of the Act to obtain a windfall, and it similarly prevents obligated spouses from using the Act to the detriment of creditors. The judicial result in *In re Sweitzer*, 111 B.R. 792 (Bankr. W.D. Wis. 1990), appears to be consistent with this statute.

## **B. Wisconsin Marital Property Taken to a Common Law State Upon Change of Domicile to the Common Law State [§ 13.18]**

### **1. In General [§ 13.19]**

The transfer of movable community property (including marital property) to a common law jurisdiction as a result of a change of domicile can produce equally perplexing problems. The issue is well stated in the *Washington Community Property Deskbook* § 8.50 (Wash. State Bar Ass'n 2d ed. 1989):

Community property brought into common law states has not fared well with respect to its preservation of identity. In a number, perhaps the majority, of cases, mere lack of familiarity by common law lawyers with the community property concept has been responsible for the proper questions not even being asked, and rights not being protected.

For a detailed discussion of the leading cases, see also McClanahan, *supra* § 13.9, § 13:12, at 591–602; Reppy & Samuel, *supra* § 13.16, at 369–75.

Although the basic choice-of-laws principles in Restatement sections 234, 258, and 259 (discussed in sections 13.9 and .10, *supra*) apply equally to situations in which community property is brought to a common law state, surprisingly few decisions have applied these principles. Some confusion stems from the fact that courts in common law jurisdictions are fond of stating that the concept of community property is unknown to their substantive law, even though the spouses' rights in the property are not terminated. *See In re Estate of Warburg*, 237 N.Y.S.2d 557 (Sur. Ct. 1963) (applying German law); *Schneider v. Toledo Trust Co. (In re Estate of Kessler)*, 203 N.E.2d 221 (Ohio 1964). Consequently, courts in common law jurisdictions have used a variety of fictions, such as constructive trusts and resulting trusts, to protect the community property interest of a nontitled spouse. *See Quintana v. Ordono*, 195 So. 2d 577 (Fla. Dist. Ct. App. 1967); *Depas v. Mayo*, 11 Mo. 314 (1848); *Edwards v. Edwards*, 233 P. 477 (Okla. 1924). These cases imply that community property undergoes an immediate conversion to a common law form of ownership. *Reppy & Samuel, supra* § 13.16, at 368; *see also Estabrook v. Wise*, 348 So. 2d 355, 357 (Fla. Dist. Ct. App. 1977) ("Florida is not a community property state, and thus is not required to recognize an encumbrance predicated upon a foreign state's community property law.").

Wisconsin wrestled briefly with these problems in *Fuss v. Fuss*, 24 Wis. 256 (1869). The Wisconsin Supreme Court refused to apply the equitable maxim that the character of property acquired in the original marital domicile will be preserved when it is used to purchase property in a subsequent marital domicile. The court also refused to enforce an agreement executed in the original marital domicile that provided, much like will-substitute agreements discussed at sections 7.99–.105, *supra*, that all property owned by either party would belong to the survivor upon the first death. It is unlikely that the *Fuss* decision would be followed today.

Only a few decisions from common law jurisdictions have taken a less anti-community property view and have recognized the legal attributes of community property brought into their jurisdictions. *Dunbar v. Bejarano*, 358 P.2d 866 (Colo. 1961) (recognizing surviving spouse's community property rights in pension benefit for purposes of avoiding inheritance tax); *Wallack v. Wallack*, 88 S.E.2d 154 (Ga. 1955) (recognizing attributes of Texas community property). *But see Schneider*, 203 N.E.2d at 226 (Ohio 1964) (holding that change of domicile from community property state to common law state did not

affect wife's rights in community property previously acquired and brought to new domicile, but exclusive management rights of husband rendered entire value of community property held in his name taxable for state inheritance-tax purposes); *Commonwealth v. Terjen*, 90 S.E.2d 801 (Va. 1956) (holding that full value of home, titled in wife's name and purchased in common law state with money brought from community property state, constituted transfer of exclusive property rights from husband and was fully subject to gift tax).

Several federal income tax cases have held that after spouses move to a common law jurisdiction, ordinary income or capital gain from community property will continue to be treated as owned equally by each spouse for purposes of filing separate federal income tax returns. *Johnson v. Commissioner*, 88 F.2d 952 (8th Cir. 1937); *Phillips v. Commissioner*, 9 B.T.A. 153 (1927); *see also Hammonds v. Commissioner*, 106 F.2d 420 (10th Cir. 1939) (holding that Texas oil interests acquired as compensation for personal services by a spouse domiciled in Oklahoma, a common law state that recognizes the earnings of the wife as separate, were governed by Texas law and characterized as community property).

As with a change of domicile from a common law to a community property state, the events of death, dissolution of the marriage, and assertion of a creditor's claim often provide the occasion for applying choice-of-laws principles. If UMPA is more widely adopted, it will be desirable for the appellate courts in common law jurisdictions to develop greater sensitivity to the appropriate choice-of-laws rules regarding characterization of property and debt.

## **2. Death of a Spouse [§ 13.20]**

A number of decisions from common law jurisdictions have misinterpreted the nature of community property brought into the jurisdiction by the spouses before one of them died. Typically, these decisions have involved inheritance tax determinations. *See, e.g., In re Hunter's Estate*, 236 P.2d 94 (Mont. 1951); *Schneider v. Toledo Trust Co. (In re Estate of Kessler)*, 203 N.E.2d 221 (Ohio 1964); *Commonwealth v. Terjen*, 90 S.E.2d 801 (Va. 1956).

An answer to the perplexing and inconsistent treatment of community property at death by common law jurisdictions has been sought through

legislation. The Uniform Disposition of Community Property Rights at Death Act, 8A U.L.A. 213 (2003) [hereinafter Uniform Disposition Act], promulgated by the National Conference of Commissioners on Uniform State Laws in 1971, is designed for adoption by common law jurisdictions and provides for the survival and recognition of basic community property attributes. The Uniform Disposition Act provides that at death, personal property wherever situated, and real property situated in the adopting state, that was acquired as or with community property becomes one-half the property of the decedent and one-half the property of the surviving spouse. The decedent's one-half is not subject to dower, curtesy, or statutory elective rights. Note that the Uniform Disposition Act does not create a new statutory category of property called community property; rather, it provides a mechanism for the succession of property that is derived from or traceable to community property.

To date, the Uniform Disposition Act has been adopted by 14 states: Alaska, Arkansas, Colorado, Connecticut, Florida, Hawaii, Kentucky, Michigan, Montana, New York, North Carolina, Oregon, Virginia, and Wyoming. The Uniform Disposition Act and comments are reproduced in full at section 13.51, *infra*.

The policy of the Uniform Disposition Act regarding treatment of community property seems clearly correct. Accordingly, the courts of those common law jurisdictions that do not legislatively adopt it should embrace its approach by judicial decision if the appropriate case arises.

### **3. Divorce [§ 13.21]**

The cases involving divorce decrees—*Estabrook v. Wise*, 348 So. 2d 355 (Fla. Dist. Ct. App. 1977); *Wallack v. Wallack*, 88 S.E.2d 154 (Ga. 1955); and *Depas v. Mayo*, 11 Mo. 314 (1848)—were all actions to divide community property located in a common law jurisdiction *following* entry of a divorce decree in the community property jurisdiction. The forthright approach in *Wallack*, which recognizes the survival of community property attributes without resorting to legal fictions, is a good one.

In *Moore v. Ferrie*, 18 Cal. Rptr. 2d 543 (Ct. App. 1993), the court was confronted with the issue of disposing of a community property asset omitted from a divorce judgment in a common law jurisdiction.

The California court acted to divide and allocate community property rights in the husband's pension on the ground that the pension had been omitted from the divorce proceedings in Ohio, a common law jurisdiction. The facts were as follows. The husband had been working for United Airlines since 1965, at which time the couple lived in California. In 1977 the husband moved to Ohio, and the wife joined him there in early 1978. In 1979, the parties separated, and the wife returned to California. In 1980, the husband filed a divorce action in Ohio. Several days later, the wife filed a petition for dissolution in California. After considerable legal skirmishing, including appeals, in both states, the husband eventually obtained a divorce judgment in Ohio. Most of the orders entered by the California court were vacated in deference to the Ohio divorce judgment. However, the California dissolution action itself was never formally dismissed.

When the former wife learned of the husband's retirement in 1991, she filed an order to show cause in the still-pending California dissolution action seeking division of the husband's pension as an omitted asset. The trial court found that it had jurisdiction to divide the community property interest in the pension. The California Court of Appeals agreed, holding that the community property portion of the pension was subject to division in California notwithstanding the earlier Ohio divorce judgment. Under *Henn v. Henn*, 605 P.2d 10 (Cal. 1980), a former spouse may maintain an action to establish his or her community property interest in a pension that was not adjudicated in an earlier final divorce decree. The community property interest in a pension is not altered except by judicial decree or agreement between the parties, and the former spouse is not collaterally estopped from litigating his or her community property interest in the pension by failing to assert this right when his or her entitlement to other community assets was adjudicated.

In *Moore*, the California Court of Appeals rejected the husband's argument that the wife's action constituted a collateral attack on the Ohio judgment, stating that an action to divide an omitted asset does not seek to modify or reopen the previous final judgment. The court pointed out that the wife did not lose her community property interest in the pension when the spouses moved to Ohio because, under Ohio law, community property does not lose its character by virtue of a move to the state. See *Schneider v. Toledo Trust Co. (In re Kessler's Estate)*, 203 N.E.2d 221 (Ohio 1964). Accordingly, if the Ohio court did not adjudicate the parties' interests in the pension, the wife retained her interest in the community property portion following the divorce as a tenant in

common. Division of this asset by a California court would not deny the Ohio judgment full faith and credit because that judgment did not purport to deal with the pension.

Allowing the wife to maintain an action to divide the unadjudicated community property pension would give the Ohio judgment no less effect than it would have in Ohio. Although Ohio law at the time did not allow the reopening or modification of a final divorce judgment to dispose of omitted property, it appeared to the court that under Ohio law, if a divorce decree became final without having disposed of certain assets, the parties were simply left with the status quo, and an unadjudicated asset remained the property of the party in whose name it was held. If an Ohio divorce decree failed to dispose of an asset held jointly by the spouses, Ohio presumably would have to allow a subsequent partition action to divide the parties' interests. Under *Schneider*, community property is a form of jointly held property that must be divided in that manner.

Although the court acknowledged that it could find no Ohio precedent addressing the precise question of the appropriate remedy when an Ohio judgment fails to dispose of a community property asset, the court said that it would assume that Ohio law was not out of harmony with California law since, under the rule of *Schneider*, the community property remains community property despite a move to Ohio. The court assumed that Ohio also would accept the corollary principle that unadjudicated community property assets remain jointly owned by the parties as tenants in common after their divorce.

The importance of *Moore* is that, absent disposition of the husband's pension plan by a judgment of the court, the wife's community property ownership interest was not divested. Thus, because the California court had jurisdiction over the parties, it was appropriate for the court to determine and allocate the respective property interests of the former spouses in the pension plan. The case is particularly interesting because it applied an Ohio decision (*Schneider*) to recognize the ongoing attributes of community property removed to a common law jurisdiction and built on that recognition to protect the community property interest of the nonemployee spouse.

No decision of a common law forum seeking to apply choice-of-laws principles in a divorce to community property brought into the jurisdiction has been found. This might be because the vast majority of

states now have equitable property division statutes that apply in divorce. In equitable division jurisdictions, the characterization of property under choice-of-laws rules no longer has much significance, regardless of whether the forum jurisdiction is a common law or community property state. Rather, the inquiry is much more likely to focus on whether the property was received as an inheritance or gift or is traceable to property received by inheritance or gift; in such cases, it is probably not subject to division. Only in those jurisdictions lacking equitable-division statutes will choice-of-laws characterization problems be likely to arise at divorce.

#### **4. Assertion of Creditors' Claims [§ 13.22]**

The relevant choice-of-laws principles are discussed at section 13.17, *supra*. Applying those principles, a creditor should be able to recover for community (or family-purpose) debts incurred in a community property jurisdiction even if the spouses move to a common law jurisdiction.

### **C. Investment of Common Law Solely Owned Property in Wisconsin Real Estate by Persons Domiciled in a Common Law State [§ 13.23]**

#### **1. In General [§ 13.24]**

The classification scheme of the Wisconsin Marital Property Act does not apply to real estate or other immovables acquired in Wisconsin unless both spouses are domiciled here. Section 766.31(8) states that the enactment of chapter 766 does not alter the classification and ownership rights of predetermination date property, except as otherwise provided in chapter 766. The determination date is defined as the last to occur of marriage, 12:01 a.m. on the date that both spouses are domiciled in Wisconsin, or 12:01 a.m. on the effective date of chapter 766 (January 1, 1986). Wis. Stat. § 766.01(5). Because, by definition, spouses domiciled elsewhere have not established a domicile in Wisconsin, no determination date applies to them, and all their property is treated as acquired before the determination date. Real estate and tangibles acquired in Wisconsin thus carry the classification and ownership rights that they would have in the absence of the Act.

This may bring into play the choice-of-laws principles of Restatement sections 234, 258, and 259 (discussed at sections 13.12–.17, *supra*). *See also* McClanahan, *supra* § 13.9, § 13.8. The decided cases invariably have involved real estate because, under the general rule that movables follow the person, movables located in one state but owned by spouses residing in another are considered to be situated in the state of domicile and to derive their property-law characteristics under its laws. *See, e.g., In re Succession of Dunham*, 408 So. 2d 888 (La. 1981).

## 2. Death of a Spouse [§ 13.25]

As noted, the Act does not apply to real estate acquired in Wisconsin by spouses unless both are domiciled here. Wis. Stat. §§ 766.01(5), .31(8). Furthermore, upon the death of a nondomiciliary spouse, there will be no augmented deferred marital property election for Wisconsin real estate because, under section 861.02(7)(a), the election applies only if the decedent spouse “is domiciled in this state.”

Real estate owned by a decedent domiciled elsewhere is therefore likely to be considered to have the characteristics of the property from the domiciliary jurisdiction that was used to acquire it. *Stephen v. Stephen*, 284 P. 158 (Ariz. 1930) (holding that real estate purchased in Arizona by a married resident of a common law state was solely owned property and not community property); *see also In re Estate of Warner*, 140 P. 583 (Cal. 1914). The Reporter’s Note to Restatement section 234 indicates that in disputes between the spouses alone, this will normally be the result. When third parties such as transferees are involved, courts of the situs of the property may be more inclined to apply their local law. *Marshburn v. Stewart*, 240 S.W. 331 (Tex. Civ. App. 1922), *aff’d*, 260 S.W. 565 (Tex. 1924).

However, in *McCarver v. Trumble*, 660 S.W.2d 595 (Tex. App. 1983), the presence of third parties did not result in application of local law. Spouses who were domiciled in Colorado, a common law jurisdiction, acquired an undivided one-half interest in Texas real estate using property supplied by each of them. Third parties owned the remaining one-half interest. The deed recited that the spouses were taking title as joint tenants with right of survivorship and also plainly stated that they were Colorado residents. After the husband died, his sons by a former marriage sold the one-fourth interest purporting to belong to him under Texas community property law to others. In an



action to quiet title, the court upheld the surviving wife's contention that she was entitled to the entire one-half interest by right of survivorship, noting that this was not an invalid attempt under Texas law to create a joint tenancy with a right of survivorship using community property but instead a transaction involving the purchase of Texas land by Colorado residents using separate funds as determined under Colorado law. This was sufficient to create a joint tenancy under Texas law. As a result, title to the entire undivided one-half interest vested in the surviving spouse by right of survivorship.

Because Wisconsin has no statutory elective rights available to the surviving spouse of a nondomiciliary decedent (and arguably has no common law rights of dower and curtesy that would apply), a problem might arise if a nonresident attempted to wholly or partially disinherit his or her spouse by acquiring Wisconsin realty with solely owned property from the domiciliary jurisdiction. The 1985 Trailer Bill created section 861.20(1) to deal with this problem. It provides an elective right for the surviving spouse of a nondomiciliary who dies leaving a valid will disposing of real property in Wisconsin that is not marital property or community property. The survivor's election consists of the same right to elect to take a portion of or an interest in property against the decedent's will that would have been available to the surviving spouse if the property were located in the jurisdiction of the decedent's domicile at the time of the decedent's death. This provision is based on a similar California statute, section 120 of the California Probate Code. Section 861.20(1) further specifies that the domiciliary state's procedure for electing against the will applies to the election.

A second section, section 861.20(2), deals with the same basic facts (i.e., a nondomiciliary decedent owning Wisconsin real estate acquired with common law solely owned property) in the context of intestate succession. Again, the statutory solution is to apply the intestate-succession law of the domiciliary jurisdiction as if the property were located in the decedent's domicile at the decedent's death.

### **3. Divorce [§ 13.26]**

No divorce cases have been found that deal specifically with real estate acquired in a community property state by common law domiciliaries. This may be explained by the relatively long-standing existence of "just and equitable" property division statutes in common

law jurisdictions, enabling divorce courts to reach any property owned by the spouses. This is in contrast to community property jurisdictions, which often can divide only the community property. Another reason for the absence of such cases may be that the issue is treated as one governed by the divorce law of the forum. *See, e.g., Latterner v. Latterner*, 8 P.2d 870 (Cal. Ct. App. 1932). As one commentator has stated,

The absence of authority on the question indicates that it is generally understood that the issue [of division of property in a divorce action] is governed by the law of the forum, since an assertion that the law of some other state governed would probably be resisted and lead to an appellate court decision on the point.

Marsh, *supra* § 13.9, at 142. A final reason for the absence of authority may be that the court of the divorce forum exercises personal jurisdiction over the parties and is able to divide property interests and compel transfers of the parties' property regardless of where the property is situated.

Cases dealing with the reverse of this topic—that is, divorce divisions of community property located in common law jurisdictions and owned by residents of a community property state—are treated at section 13.34, *infra*.

#### **D. Investment of Marital Property in Real Estate in a Common Law State by Persons Domiciled in Wisconsin [§ 13.27]**

##### **1. In General [§ 13.28]**

Once again, the relevant choice-of-laws considerations are set forth in Restatement sections 234, 258, and 259 (discussed at sections 13.9–10, *supra*). For reasons discussed at section 13.24, *supra*, the cases will ordinarily involve realty.

## **2. Death of a Spouse [§ 13.29]**

### **a. In General [§ 13.30]**

Despite a dearth of cases, it is expected that when only the spouses are involved, the courts of the situs will look to the nature of the property used to acquire the real estate in making the appropriate choice of law. *See supra* § 13.25.

### **b. Marital Property Rights [§ 13.31]**

Under proper conflict-of-laws analysis, courts in common law jurisdictions must recognize a surviving nondomiciliary spouse's vested, one-half Wisconsin marital property interest in real estate located in the common law jurisdiction if the real estate was acquired in whole or in part with marital property. If the common law state where the real estate is located has adopted the Uniform Disposition Act (discussed at section 13.20, *supra*), this result will be dictated by statute. Example 2 in the comment to section 1 of the Uniform Disposition Act indicates that the Act will apply to real estate located in an enacting jurisdiction that is owned by a nondomiciliary but acquired with or traceable to community property. 8A U.L.A. at 195.

Less clear is whether such important rights of succession as the revised and expanded intestate succession rights of a surviving spouse under section 852.01(1)(a), or the surviving spouse's elective share in augmented deferred marital property at death under section 861.02, will be recognized by the common law situs jurisdiction. Sections 236 and 241 of the Restatement indicate that questions of the devolution of interests in land upon the intestate death of the owner and the existence and extent of common law or statutory interests of a surviving spouse in land are determined by the law that would be applied by the courts of the situs. Usually that will be the local law of the situs. Accordingly, courts in common law jurisdictions that follow the Restatement position may ignore Wisconsin's intestate succession law and augmented deferred marital property rule in favor of applying their own statutory rights or elections. *See, e.g., Spence v. Spence*, 195 So. 717 (Ala. 1940); *Ehler v. Ehler*, 243 N.W. 591 (Iowa 1932); *Sinclair v. Sinclair*, 109 A.2d 851 (N.H. 1954).

Possible procedural solutions for the difficulties that might be faced in convincing the courts of another state to recognize Wisconsin marital property interests in real estate located there have been suggested by Professor June M. Weisberger in *Selected Conflict of Laws Issues in Wisconsin's New Marital (Community) Property Act*, 35 Am. J. Comp. L. 295, 302 (1987). Assuming that real estate in the other state is titled solely in the name of either the decedent spouse or the surviving spouse (so that the title does not reflect the actual ownership interests), the Wisconsin probate court having jurisdiction over the decedent's estate might order either the decedent's personal representative (if the real estate is titled in the decedent's name) or the Wisconsin surviving spouse (if the real estate is titled in the surviving spouse's name) to execute and record a conveyance in the situs state to reflect the ownership rights of the parties under Wisconsin law. This would follow logically from the probate court's authority in section 857.01 to determine the classification of property and to render a decree that property be titled in accordance with its classification.

Weisberger also suggests the use of a court proceeding modeled on traditional proceedings to quiet title in which the rights of various parties having an interest in real estate are determined on the basis of personal jurisdiction over them. Under this approach, if the Wisconsin court obtains jurisdiction over all the interested parties, its judgment should be entitled to full faith and credit in the state where the real estate is located.

### **c. Deferred Marital Property Rights [§ 13.32]**

It is instructive to examine some of the issues that the courts of a common law jurisdiction will face in deciding whether to apply the section 861.02 elective share in deferred marital property to real estate located in another state but owned by a Wisconsin married person. Consider the following situation:

➤ **Example.** A spouse using her wages acquires real estate located in Minnesota during marriage but before the effective date of the Act. All these wages would have been marital property for purposes of the deferred marital property reach-back of sections 851.055 and 861.02. Both spouses are domiciled in Wisconsin at all relevant times, including on the date of acquisition of the realty and the date of the acquiring spouse's death. The acquiring spouse's will leaves the Minnesota real estate to third persons. The surviving spouse files a

petition to make the augmented deferred marital property election under section 861.08(1), claiming an amount equal to 50% of the augmented deferred marital property estate. Under section 861.02(2)(b), the augmented deferred marital property estate includes real property located in another jurisdiction. Assume that some portion of the Minnesota real estate must be used to satisfy the elective share, and that the devisees of the Minnesota real estate are given appropriate notice of the proceedings. The court enters a judgment requiring the devisees to make a prorated contribution toward the surviving spouse's augmented deferred marital property elective share. The surviving spouse seeks to enforce the judgment against the devisees in Minnesota.

Applying the basic choice-of-laws principles of Restatement section 6 does not lead to a clear-cut answer as to what a Minnesota court would do. A Minnesota court might determine that Wisconsin has the most significant relationship to the parties and enforce the judgment for an augmented deferred marital property elective-share contribution against the third persons. Or, because the real estate is located in Minnesota, the court might apply the Minnesota statutory election against the will instead of the Wisconsin augmented deferred marital property elective share on the ground that it will further certainty, predictability, and uniformity of result.

#### **d. Rights to Income from Real Estate [§ 13.33]**

Even more difficult than deciding whether the court would apply Wisconsin's deferred marital property elective share is characterizing the income from the real estate in the above example. Will the income be classified as marital property under the income rule of section 766.31(4) or classified as common law solely owned property? The answer depends on whether the income is deemed to be converted to personal property and "repatriated" to Wisconsin under the doctrine that movables follow the person, *see, e.g., Succession of Packwood*, 9 Rob. 438 (La. 1845), or is viewed merely as an incident of the real estate. With the spouses' strong relationship to Wisconsin, repatriation and classification of the income as marital property would be equitable. The result might be different, however, if the income were directly plowed back into the real estate through payments on a purchase money mortgage with a Minnesota bank or a land contract with a Minnesota vendor. Under those circumstances, persons domiciled in Minnesota would have a stake

in the dispute, and applying Wisconsin law might disrupt justified expectations of the parties.

*Commissioner v. Skaggs*, 122 F.2d 721 (5th Cir. 1941), illustrates the complexity of these questions. In that case, spouses resided in Texas; before marriage, the husband acquired income-producing real estate in California. The question was whether the income from the property should be treated as community property under Texas law (which has an income rule similar to Wisconsin's) or as separate property under California's community property law. Applying the law of the situs (California), the court said that the income was the husband's separate property. Reppy and Samuel, *supra* § 13.16, at 354, offer an excellent analysis of this case, noting the possible results depending on the conflict-of-laws methodology used by the forum state. Their analysis suggests that a forum that, like Wisconsin, has a "better law" factor in its conflicts methodology would have applied Texas law because of its broader view of marital sharing.

### 3. Divorce [§ 13.34]

A number of decisions recognize that community property invested in real estate in a common law jurisdiction by one spouse will not lose its community property characteristics and therefore is equally divisible in the event of divorce. These decisions customarily have come from the divorce courts of the community property jurisdiction where the parties were domiciled rather than from the courts of the state where the land was situated. The cases have uniformly recognized that while the domiciliary courts were not able to directly affect title to the out-of-state property, they were free to control its disposition by exercising in personam jurisdiction over the spouses. *Noble v. Noble*, 546 P.2d 358 (Ariz. Ct. App. 1976); *Fink v. Fink*, 603 P.2d 881 (Cal. 1979); *Rozan v. Rozan*, 317 P.2d 11 (Cal. 1957); *Tomaier v. Tomaier*, 146 P.2d 905 (Cal. 1944); *Economou v. Economou*, 274 Cal. Rptr. 473 (Ct. App. 1990); *Glaze v. Glaze*, 605 S.W.2d 721 (Tex. Civ. App. 1980); *see also Grappo v. Coventry Fin. Corp.*, 286 Cal. Rptr. 714 (Ct. App. 1991); *Haws v. Haws*, 615 P.2d 978 (Nev. 1980) (in *Grappo* and *Haws*, courts determined rights in Nevada real estate, purchased by one spouse with separate property while both spouses were domiciled in California, under community property laws of California, not Nevada).

The Wisconsin Supreme Court has also recognized that in personam orders to parties under its jurisdiction may affect out-of-state property. *Dalton v. Meister*, 71 Wis. 2d 504, 239 N.W.2d 9 (1976). It seems likely that a court would seek to achieve similar results in divorce property settlements under section 767.61. *See also Belleville State Bank v. Steele*, 117 Wis. 2d 563, 345 N.W.2d 405 (1984) (requiring that judgment of Illinois divorce court ordering party to convey Wisconsin real estate be enforced); *Bailey v. Tully*, 242 Wis. 226, 7 N.W.2d 837 (1943) (enforcing California decree ordering conveyance of Wisconsin real estate from one party to the other).

For additional discussion concerning the means by which a forum divorce court may exercise its equitable powers to protect its domiciliaries at the time of divorce, see Weisberger, *supra* § 13.31, at 297–98.

In *Fall v. Eastin*, 215 U.S. 1 (1909), the U.S. Supreme Court recognized the power of a divorce court in the state of Washington (where the parties were domiciled) to compel the former husband to execute a conveyance of land located in Nebraska as part of the equitable division of the parties' assets. The former husband conveyed the land to a third person in fraud of the wife's interest under the decree. The wife commenced an action in Nebraska against the purchaser to quiet title to the land. The Court declined to give independent substantive effect to the Washington decree as a document of title affecting the real estate in Nebraska under the full faith and credit clause of the U.S. Constitution, stating that the appropriate remedy under the circumstances was a contempt citation against the husband by the Washington court. *See also* Sheldon R. Shapiro, Annotation, *Power of Divorce Court to Deal with Real Property Located in Another State*, 34 A.L.R.3d 962 (1970), and cases cited therein.

#### **4. Remedies During Marriage [§ 13.35]**

A question somewhat related to those arising in a divorce action is whether courts in a common law jurisdiction where real estate acquired with Wisconsin marital property is located would grant any of the interspousal remedies of subsections 766.70(3) and (4), particularly those adding the name of the other spouse, altering the management and control rights of the property, or changing its classification.

➤ **Example.** Real estate is acquired in Florida with Wisconsin marital property and titled in the name of one spouse. Subsequently, an action is brought in Florida by the nontitled spouse, who resides in Wisconsin, seeking to change the title to his or her name under section 766.70(4). The whereabouts of the titled spouse is unknown.

The essential question relates to the nature of the Florida court's jurisdiction over the matter. Assuming that the location of the real estate confers a legal basis for a spouse claiming an ownership interest to invoke the jurisdiction of the Florida courts, the Florida court could hear the matter. The proceeding may be characterized as quasi in rem. *See* Restatement ch. 3 introductory note to topic 2 (Judicial Jurisdiction Over Things).

The Florida court might then consider remedies relating to the title or reclassification of the real estate. If the spouses are considered domiciled in Wisconsin, and Florida's conflict-of-laws methodology determines that Wisconsin has the dominant interest, Florida might choose to apply Wisconsin's statutory remedies to real estate acquired with marital property. Restatement § 8 cmt. k.

If the matter arose in Wisconsin, and if the court could obtain in personam jurisdiction over the parties, the court could apply remedies by issuing orders to the parties that would affect the Florida real estate acquired with marital property, *see Dalton v. Meister*, 71 Wis. 2d 504, 239 N.W.2d 9 (1976); Restatement § 55, although subsequent proceedings to enforce the judgment in Florida might be required.

## **5. Assertion of Creditors' Claims [§ 13.36]**

The choice-of-laws principles applicable to contract creditors' rights include those discussed in Restatement section 188. *See supra* § 13.6. One bankruptcy court decision is illustrative. In *Janis v. Janis (In re Janis)*, 125 B.R. 274 (Bankr. D. Ariz. 1991), a creditor under a guaranty attempted to enforce a second mortgage against a Hawaii condominium owned by the debtor spouses, both of whom were Arizona residents. The bankruptcy trustee moved to set aside the Hawaii foreclosure judgment and invalidate the creditor's claim against the equity in the condominium. It appeared that only the husband had executed the guaranty obligation, but that the wife had joined in the second mortgage securing it. Arizona law requires that both spouses join in a transaction



of guaranty in order for the spouses' community property to be bound. *See* Ariz. Rev. Stat. § 25-214 (current through legislation effective February 9, 2010 of the Sixth Special Session, and legislation effective April 16, 2010 of the Second Regular Session of the Forty-Ninth Legislature (2010)).

After examining the applicable principles of Restatement section 188, the Bankruptcy Court concluded that because Arizona had the most significant relationship to the parties, Arizona law would be applied in determining the enforceability of the guaranty. The court held that, under Arizona law, because the wife had not joined in the guaranty, it was effective only as to the husband and would ordinarily be recoverable only from his separate property. The court also concluded that because the debtors at all times were Arizona residents, the Hawaii condominium should be regarded as their community property. After noting that Hawaii at one time had been a community property jurisdiction and still had laws on its books to avoid divestiture of community property rights or interests, the court concluded that Hawaii would treat the condominium as community property under its law.

The U.S. District Court subsequently reversed the decision of the bankruptcy court. *Janis v. Janis (In re Janis)*, 151 B.R. 936 (Bankr. D. Ariz. 1992). The court held that the wife's joining in the second mortgage on the Hawaii condominium to secure her husband's guaranty satisfied the spousal joinder requirement under the Arizona statutes. In addition, her execution of the second mortgage constituted an independent promise of payment, because the mortgage explicitly referred to payment of the guaranty and the husband's underlying obligations, for which it was security. Accordingly, the court held that the second mortgagee could recover from all the remaining proceeds from sale of the condominium, not just from the husband's share.

### **E. Transfers of Property Between Wisconsin and Other Community Property Jurisdictions [§ 13.37]**

Not all transfers of property into or out of Wisconsin pursuant to a change of domicile will involve common law property states. Some will inevitably involve property brought to Wisconsin from a community property state or taken to a community property state from Wisconsin. Because of variations in the characteristics of community property under the laws of the original eight community property states, as well as

differences between the community property of those states and Wisconsin's marital property, conflict-of-laws problems may arise.

For example, assume that California civil law separate property (i.e., property acquired before marriage or during marriage by gift or inheritance) is brought to Wisconsin by a spouse who establishes marital domicile here. The spouse then invests in Wisconsin income-producing real estate. The income from separate property under California's community property law remains separate. How is the income treated under the Act? Section 766.31(8) purports to preserve the classification and property rights of the California separate property. A problem arises, however, because of the "except as provided otherwise in this chapter" language of section 766.31(8). The comment to UMPA section 4 indicates that the income treatment in subsection 4(d) (which became section 766.31(4)) is one exception to the basic rule. Thus, the income from the California separate property will be classified as Wisconsin marital property unless the owner spouse acts unilaterally to reclassify the income as individual property under section 766.59. If this is not done, and if the income is used to pay the mortgage or for other capital purposes, the mixed property rule of section 766.63(1) would apply and tracing would be necessary to determine the separate property component. The original California separate property component would not be subject to the augmented deferred marital property election of section 861.02 at death because it would not have been marital property under the Act. *See* Wis. Stat. § 766.31(6), (7).

The following example illustrates another conflict-of-laws problem involving a community property state:

➤ **Example.** A married couple establishes domicile in Wisconsin after having resided for a number of years in Arizona. They bring with them a life insurance policy on the life of one spouse that names that spouse's child by a prior marriage as beneficiary. The insured spouse is the record owner of the policy. Premiums from the inception of the policy were paid entirely with inherited civil law separate property while the spouses were domiciled in Arizona. Arizona (along with New Mexico, Texas, and Louisiana) employs an "inception of title" rule for classifying life insurance policies. This rule provides that if the policy was initially acquired with the separate property of one spouse, it remains the separate property of that spouse even if premiums are subsequently paid with community property. The community is deemed to have a lien against the policy and the

proceeds for the amount of premiums paid with community property. Although the insured spouse intends to continue the practice of paying the premiums out of inherited property after establishing domicile in Wisconsin, several premiums are inadvertently paid with Wisconsin marital property. Subsequently, after residing in Wisconsin for a time, the insured spouse dies.

Because a premium has been paid with Wisconsin marital property, under Wisconsin law the time-based apportionment rule of section 766.61(3)(b) would determine the marital property component of the life insurance proceeds. This conflicts with the Arizona inception-of-title rules as buttressed by the preservation of property rights provisions of section 766.31(8). The court must decide which state's law will apply.

Assume now that the insurance policy in the preceding example is on the life of a child and is owned by the spouse who is the child's parent. Under these facts, section 766.61 will not apply, and it will be necessary to resort to the general rule of Restatement section 259 that the law of the marital domicile when an intangible is acquired continues to govern its characterization after it is removed to another jurisdiction. Section 766.31(8) purports to protect that classification. But, if some premiums on such a policy are paid with Wisconsin marital property after the spouses' determination date, a conflict may arise if the mixed property presumption and tracing rules of section 766.63(1) apply. If the Wisconsin court determines that section 766.63(1) is an exception to the preservation-of-property-rights rule of section 766.31(8), and if the child dies or the policy is surrendered after the move to Wisconsin, does the court apply Arizona law and merely restore to marital property the premiums paid from marital property in a manner consistent with the inception-of-title rule, while awarding the balance of the proceeds to the parent who owns the policy? Or does it determine that Wisconsin law applies, with a further requirement of equitable apportionment of the proceeds? If it determines that apportionment is appropriate, does it use the time-based rule of section 766.61(3)(b), or does it apportion the proceeds based on the ratio of marital property premiums to total premiums? There is, of course, no way of knowing how the Wisconsin courts will deal with these issues. Suffice it to say all the theories are plausible, and each has advantages and disadvantages.

Next, assume that the policy in the above example is owned by the spouse of the insured; this spouse is named as beneficiary. The owner spouse pays the premiums from Arizona inherited separate property

while the spouses reside there and continues this practice after establishing domicile in Wisconsin. Inadvertently, however, several premiums are paid with marital property. Upon the death of the insured, the insurance proceeds would be treated entirely as the individual property of the surviving owner spouse under section 766.61(3)(c), even though several premiums were paid with Wisconsin marital property. If the insured decedent's will leaves his or her estate to a child of a prior marriage, the insured's estate might have a lien or right to reimbursement from the beneficiary spouse under Arizona law and section 766.31(8) for one-half of the premiums paid with marital property. A court may be asked to determine which set of rules applies.

Conflicts regarding insurance policies will also occur if the spouses' former domiciliary state determines ownership of the policy or the proceeds under an apportionment rule based on the ratio of premiums paid with community funds to the total amount of premiums paid. California and Washington follow such a rule. If all premiums were paid out of inherited civil law separate property both before and after the spouses changed domicile to Wisconsin, except for several premiums inadvertently paid out of Wisconsin marital property, the conflict-of-laws problem becomes evident. The statutory time-based apportionment rule of section 766.61(3)(b) may produce a far different result than an apportionment based on the ratio of premiums paid with community funds (i.e., marital property) to the total amount of premiums paid. The latter apportionment formula is arguably an element of the property rights preserved by section 766.31(8).

Note that in most of the above examples the election against the augmented deferred marital property estate under section 861.02 would not apply, because premium payments on the policy before the establishment of the spouses' domicile in Wisconsin were made from property that would not have been marital property. It is much more likely that spouses moving to Wisconsin who bring with them insurance policies they own on the life of a spouse (or a child) will have paid premiums with earnings or income that clearly would have been Wisconsin marital property if the Act had applied to the spouses from the inception of their marriage. These policies would constitute deferred marital property as defined by sections 851.055 and 861.02(2)(b). Under these circumstances, the election against the augmented deferred marital property estate under section 861.02 may enable a surviving spouse to reach part or all of the value of the policies.

Retirement benefits generate the same kinds of choice-of-laws problems as life insurance policies, again depending on the rules that states of former domicile (and employment) use to characterize retirement benefits. The situation is further complicated by the overlay of federal law applicable to benefits paid by qualified plans governed by ERISA (Employee Retirement Income Security Act of 1974), 29 U.S.C §§ 1001–1461. *See supra* § 2.214–.217.

The discussion up to this point has involved spouses who move from other community property states to Wisconsin. When the transactional analysis flows in the other direction, that is, the spouses move from Wisconsin to another community property jurisdiction and take Wisconsin marital property with them, there is also potential for difficult choice-of-laws questions. This is because the property law systems of other community property states tend to be far less structured and formal than the regime created by the Wisconsin Marital Property Act. As a result, it is impossible to speculate on the extent to which other community property jurisdictions will recognize particular attributes of Wisconsin marital property, such as the terminable interest of a nonemployee spouse under section 766.62(5) in retirement benefits accrued while the spouses were domiciled in Wisconsin, or the title-based management and control rules of section 766.51 for marital property. The cases and statutes of the various community property jurisdictions dealing with the treatment of “other” property brought into those states from outside, discussed at sections 13.13–.17, *supra*, point out the difficulties encountered in attempting to freely analogize between similar forms of property ownership.

Finally, many of the questions about Wisconsin residents investing marital property in real estate in a common law state, discussed *supra* §§ 13.27–36, may also arise when a Wisconsin resident uses marital property to acquire real estate in another community property jurisdiction. The community property state’s intestate-succession laws, provisions for protection of a spouse at death, and creditors’ rights and remedies may differ, perhaps significantly, from the Wisconsin scheme. Appropriate choice-of-laws principles will have to be applied when disputes arise.

## **F. Effect of Choice of Laws on Marriage Agreements**

### **[§ 13.38]**

### **1. General Principles Regarding Construction and Enforceability of Marriage Agreements [§ 13.39]**

Relatively little authority exists on which law governs the validity and construction of a marriage agreement (assuming the agreement does not contain a choice-of-laws provision) when the agreement is entered into while the spouses are domiciled in one state but enforcement is sought after they change domicile to another. Wisconsin applies a grouping-of-contacts analysis when the issue arises in its courts. *Knippel v. Marshall & Ilsley Bank (In re Estate of Knippel)*, 7 Wis. 2d 335, 96 N.W.2d 514 (1959); *see supra* § 13.6. This approach has also been followed in Ohio. *Osborn v. Osborn*, 226 N.E.2d 814 (Ohio C.P. 1966), *aff'd*, 248 N.E.2d 191 (Ohio 1969). Other states have simply applied the law of the jurisdiction where the agreement was made, *Robinson v. Shivley*, 351 S.W.2d 449 (Ark. 1961); *Fernandez v. Fernandez*, 15 Cal. Rptr. 374 (Ct. App. 1961); *Hill v. Hill*, 262 A.2d 661 (Del. Ch.), *aff'd*, 269 A.2d 212 (Del. 1970); *Chaudry v. Chaudry*, 388 A.2d 1000 (N.J. Super Ct. App. Div. 1978); *Davis v. Davis*, 152 S.E.2d 306 (N.C. 1967), or the law of the state where the agreement was performed, *Sun Life Assurance Co. v. Hoy*, 174 F.Supp. 859 (E.D. Ill. 1959) (applying Illinois law to determine that oral premarital agreement had been fully performed and thus would be enforced despite statute of frauds).

A generally accepted conflict-of-laws principle permits parties to a contract to choose the local law that will govern the construction and enforceability of the agreement. Restatement § 187. Ordinarily, courts will recognize this choice unless the chosen state has no substantial relationship to the parties or the transaction or if applying the law of the chosen state would offend some fundamental public policy of either the forum state or another state that has a materially greater interest in the matter's outcome than does the chosen state. *Id.*

An interesting and detailed discussion of these principles is found in *Estate of Richman v. Commissioner*, 68 T.C.M. (CCH) 527 (U.S. Tax Ct. 1994) involving a Texas couple's purchase of mutual-fund shares from a Massachusetts business trust using Texas community property funds. The couple opened the account as a joint tenancy with rights of survivorship, and the mutual-fund shares were held in that form. The

trust agreement and account application comprising the contract contained a choice-of-law provision reciting that the rights of all parties, and the validity and construction of all provisions, were subject to and construed according to the laws of Massachusetts. Following the husband's death, the Commissioner contended that the mutual-fund shares in fact were Texas community property, and that the decedent's one-half interest (which passed to his children) did not qualify for the federal estate-tax marital deduction under I.R.C. § 2056. The Tax Court concluded that the choice-of-laws provision in the application and trust agreement mandated the characterization of the mutual-fund shares as joint tenancy property, and that this characterization did not offend any fundamental public policy of the state of Texas. Thus, the mutual-fund shares passed by survivorship to the surviving spouse and qualified for the marital deduction.

Wisconsin courts have followed the Restatement position but not in the specific context of marriage agreements. *See State Farm Life Ins. Co. v. Pyare Square Corp.*, 112 Wis. 2d 65, 331 N.W.2d 656 (Ct. App. 1983); *First Wisconsin Nat'l Bank v. Nicolaou*, 85 Wis. 2d 393, 398 n.1, 270 N.W.2d 582 (Ct. App. 1978). However, section 766.58(3)(g) specifically recognizes that parties may choose the law governing construction of marital property agreements. Note that the statute does not mention the choice of the law that will govern validity or enforceability; it is not known whether the provision of section 766.58(3)(h) that permits spouses to agree concerning "any other matter affecting either or both spouses' property" will be construed to cover these aspects.

A marriage agreement that states a choice of law generally will be governed by the law chosen, despite a change of marital domicile. The selected law will be enforced in a subsequent domicile if the agreement expressly provides for use of the law, so long as enforcement would not violate the public policy of the subsequent domicile. *See Weisz v. Weisz*, 97 Cal. Rptr. 18 (Ct. App. 1971); *Norris v. Norris*, 419 A.2d 982 (D.C. 1980); *Hirsch v. Hirsch*, 309 So. 2d 47 (Fla. Dist. Ct. App. 1975); *Wyatt v. Fulrath*, 211 N.E.2d 637 (N.Y. 1965) (criticizing strongly, in dissent, treatment of New York depository agreements containing choice-of-laws clauses like express marriage agreement between spouses, when spouses were Spanish citizens and domiciliaries who never came to New York); *Behr v. Behr*, 266 S.E.2d 393 (N.C. Ct. App. 1980); *Rogers v. Rogers*, 373 A.2d 507 (Vt. 1977); *McGill v. Hill*, 644 P.2d 680 (Wash. Ct. App. 1982). *But see Scherer v. Scherer*, 292 S.E.2d 662 (Ga. 1982)

(interpreting agreement under Georgia law, when both parties so stipulated, despite fact that agreement stated that it was to be construed according to Michigan law).

An issue related to inclusion of a choice-of-laws provision in a marriage agreement is the effect that the agreement will have on subsequently acquired property following a change of domicile to another jurisdiction. As stated by one commentator,

The general rule, that the law of the second jurisdiction governs marital-property interests, in subsequent acquisitions of the spouses after a change of domicile, is of course subject to modification by an express antenuptial agreement between the spouses. If the spouses agree by such a contract, which complies with the necessary formalities, that their marital property interests shall continue to be governed by the law of their first domicile even after removal to another jurisdiction, there is no reason why such an agreement should not be given effect as between the parties.

Marsh, *supra* § 13.9, at 218–19 (footnote added). (Marsh uses the term *marital-property interests* to denote a broad array of spousal property rights under both the common law and community property systems. This is not a reference to the specific property classification of that name in UMPA or the Act.)

The more difficult question, of course, is posed when the marriage agreement does not contain a choice-of-laws provision and does not mention what effect, if any, a change of marital domicile is to have on the agreement. Some cases have held that the agreement will not be enforced with respect to property acquired in the subsequent domicile unless the contract expressly provides for the contingency of change of domicile. *Fuss v. Fuss*, 24 Wis. 256 (1869); *Long v. Hess*, 40 N.E. 335 (Ill. 1895); *Hoefer v. Probasco*, 196 P. 138 (Okla. 1921); *Clark v. Baker*, 135 P. 1025 (Wash. 1913). According to Marsh, the better view is represented by those courts in a jurisdiction of subsequent domicile that have rejected such a mechanical rule and, despite the absence of an express provision, have enforced the agreement with respect to after-acquired property if that appeared to be the spouses' intent. *Sanger v. Sanger*, 296 P. 355 (Kan. 1931); *Kleb v. Kleb*, 62 A. 396 (N.J. Ch. 1905), *aff'd*, 65 A. 1118 (N.J. 1907); *Lemye v. Sirker*, 235 N.Y.S. 273 (App. Div. 1929); *Spence v. Cole*, 205 P. 172 (Okla. 1922).



## 2. Specific Considerations Regarding Enforceability of Wisconsin Marital Property Agreements [§ 13.40]

### a. Formal Requirements [§ 13.41]

Almost all states have a statute similar to section 853.05, which provides that even if a will is not executed in compliance with the formal requirements of the state where it is offered for probate, it will nonetheless be treated as validly executed if it is in writing and was executed in accordance with the law (either at the time of execution or at the time of death) of the place where the will was executed, of the testator's domicile at the time of execution, or of the testator's domicile at the time of death. However, similar statutes are not found for marriage agreements.

The formal requirements for a valid marital property agreement in Wisconsin are very simple: there must be a document, and it must be signed by both spouses. Wis. Stat. § 766.58(1). There is no need for consideration. *Id.* Other states, whether common law or community property, may require greater formalities, including witnesses, acknowledgment, and recording. See Alexander Lindey & Louis I. Parley, *Lindey and Parley on Separation Agreements and Antenuptial Contracts* §§ 90.01–20, 11.64 (2d ed. 1999); de Funiak & Vaughn, *supra* § 13.11, at § 136.

De Funiak and Vaughn make a compelling case for enforcing agreements executed in another state regardless of differences in the formal requirements:

Where the spouses at the time of the marriage, or even after the marriage, enter into an express contract governing their rights and interests in property to be acquired there is no reason why such an express agreement should not govern and be recognized in other states than that in which it is made, provided that it was valid where made and provided that its recognition and enforcement are not against the public policy of the forum.

De Funiak & Vaughn, *supra* § 13.11, at § 90; see also *Hill v. Hill*, 262 A.2d 661 (Del. Ch.), *aff'd*, 269 A.2d 212 (Del. 1970). From a choice-of-laws standpoint, then, if spouses validly execute a marital property agreement while domiciled in Wisconsin and later move to another state,

the move alone should not affect the enforceability of the agreement in the new state of domicile.

### **b. Unique Features of Will-substitute Agreements [§ 13.42]**

Conflict-of-laws questions are likely to arise regarding the multistate ramifications of will-substitute marital property agreements entered into by spouses while domiciled in Wisconsin. (See section 766.58(3)(f) and sections 7.99–.105, *supra*, for a discussion of such agreements.)

One interesting question arises when spouses domiciled in Wisconsin enter into such an agreement and subsequently change their domicile to another state, where one spouse dies. The issue is whether the agreement will be recognized as valid and given effect.

The statute authorizing will-substitute agreements is in derogation of Wisconsin's statute of wills, section 853.03, which requires certain formalities in a valid will. Virtually all other states have similar statutes of wills; relatively few have provisions in derogation of the statute of wills as broad as Wisconsin's. Washington's statutes on community property agreements, Wash. Rev. Code § 26.16.120 (current with amendments received through Jan. 15, 2010), and nontestamentary arrangements, Wash. Rev. Code § 11.02.091 (current with 2010 legislation effective through April 22, 2010), come close, but the statute on community property agreements applies only to transfers of community property at death (and not to other classifications of property). For this reason, community property agreements in Washington typically classify all or most of the property of spouses (including future acquisitions) as community property to give the agreement maximum effect. A number of other states have adopted the Uniform Probate Code, including the nontestamentary transfer provisions of section 6-101. Wisconsin has added similar statutory provisions covering a variety of nonprobate transfers, *see* Wis. Stat. §§ 705.10–.31. These are modeled after Uniform Probate Code section 6-101 (Uniform Nonprobate Transfers at Death Act) and sections 6-301 through 6-311 (Uniform TOD Security Registration Act). The Wisconsin statute dealing with nonprobate transfers at death, Wis. Stat. § 705.10, specifically includes nonprobate transfers on death by provisions in a marital property agreement.

If the married couple has moved to a jurisdiction that lacks statutory provisions validating a broad array of nontestamentary dispositions at death, the efficacy of the agreement to transfer the decedent's property located in the new domicile is likely to come into question when the first spouse dies. The spouses themselves may not have executed wills in the new domicile because they believed that their will-substitute agreement would continue to be valid. The result in such a case is very likely to depend on the nature of any statute in the state of domicile that permits transfers at death in derogation of the statute of wills. The result will also depend on the domiciliary courts' views concerning the public-policy implications of permitting transfers at death by contract—even when the contract specifies that Wisconsin law is to apply to the issues of construction and validity, and Wisconsin law clearly permits such arrangements.

Perhaps a more common situation will be that in which a Wisconsin couple enters into a will-substitute agreement that attempts to affect out-of-state real property. For reasons discussed previously, the state where the land is located may not recognize the validity of nontestamentary transfers of this sort under its own local law. If this is the case, and if the decedent spouse dies without a valid will, a court in the situs jurisdiction might then proceed to apply its own law, with the result that the land would pass by the situs state's law of intestate succession. On the other hand, if the decedent dies domiciled in Wisconsin and the surviving spouse and other interested parties also reside in Wisconsin, a case could be made that the state of the situs of the land should apply Wisconsin law and give effect to the nontestamentary transfer. *See supra* §§ 13.9, .31.

It is possible, however, that persons other than the recipient or recipients of the real estate under the terms of the will-substitute agreement would be entitled to an interest in the real estate under the intestate succession law of the state of the situs. In this situation, the courts of the situs may be reluctant to give effect to a Wisconsin will-substitute agreement unless the persons who would otherwise receive an interest in the land consent to the transfer or disclaim or renounce their interests.

The courts of the situs may also be reluctant to give effect to a Wisconsin will-substitute agreement if the rights of other third parties (such as creditors) in the situs jurisdiction would be adversely affected. The answer to this problem might be for the court in the situs jurisdiction to also recognize and apply the creditor protection provisions of section

859.18, since these are specifically intended to discourage the avoidance of creditors' rights through the use of will-substitute agreements. *See supra* § 7.12. This would permit application of Wisconsin law to accomplish the purposes of the agreement and would at the same time protect creditors' interests.

Professor Weisberger suggests that when spouses domiciled in Wisconsin have entered into a will-substitute agreement that by its terms applies to out-of-state real estate and one spouse dies, the transferee under the will-substitute agreement should be able to confirm his or her interest in the real estate in a Wisconsin proceeding under section 863.27, 865.201, or 867.046 and then record or enforce the order or judgment in the situs state. *See Weisberger, supra* § 13.31, at 304. However, section 867.046 (providing for summary confirmation of interests in property passing by will-substitute agreement) and section 865.201 (providing for confirmation of such interests in the context of informal administration) by their terms do not appear to apply to property located outside Wisconsin, although the procedures for confirmation of such interests in the context of formal probate, *see Wis. Stat.* § 863.27, may not be so limited. Furthermore, a question exists regarding whether the courts of the state where the real estate is located will give effect to such a court order or judgment as against the rights of a creditor or an intestate taker under its own laws, unless it is shown that the Wisconsin court has obtained jurisdiction over them. *See supra* §§ 13.9–10.

**c. Giving Effect to Classification of Out-of-state  
Real Estate by Marital Property Agreement  
[§ 13.43]**

The following may be a fairly common conflict-of-laws situation. Both spouses are domiciled in Wisconsin, and one spouse inherits real estate in another state. Later, the spouses enter into a Wisconsin marital property agreement classifying all their assets (including inherited assets) as marital property pursuant to section 766.31(10). The agreement is not limited in its application to assets situated in Wisconsin. No effort is made to change the title to the inherited out-of-state real estate after execution of the marital property agreement.

The question is whether the courts of the situs state will honor the classification of the real estate as co-owned marital property if the non-inheriting spouse dies first. Even if the situs state is one that has adopted the Uniform Disposition Act, *see supra* § 13.20, it is not clear whether the language of section 1 of the Uniform Disposition Act, 8A U.L.A. at 216–17, is broad enough to cover the situation, because it seemingly applies to real estate *acquired with* community property—that is, “any real property situated in this state which was *acquired with the rents, issues or income of, the proceeds from, or in exchange for, property acquired as or which became, and remained, community property* under the laws of another jurisdiction.” (Emphasis added.) If the Uniform Disposition Act does not apply (or has not been enacted in the situs state), a policy question is raised as to whether the courts of the situs jurisdiction will recognize the property classification created by the marital property agreement under section 766.31(10). The procedural solutions suggested by Professor Weisberger and discussed in detail in section 13.31, *supra*, seemingly would apply here as well. If the Wisconsin probate court having jurisdiction over the deceased spouse’s estate has jurisdiction over all the interested parties, it may compel the deceased spouse’s personal representative and the surviving spouse to execute and record a conveyance in the situs state to reflect the ownership rights of the parties under Wisconsin law.

Perhaps a simpler solution would be for spouses entering into a comprehensive marital property agreement to execute and record a conveyance of out-of-state real estate that effectively recognizes their co-ownership under local law. This at least would avoid title and conveyancing problems under the law of the situs state after the death of the first spouse. More problematic, however, is whether the Internal Revenue Service would recognize the classification of the out-of-state real estate as marital property on the strength of the Wisconsin marital property agreement, particularly if the real estate is located in a non-community property jurisdiction.

## G. Choice of Laws and Dual Domiciles [§ 13.44]

### 1. Definition of a Marital Domicile [§ 13.45]

#### a. Before May 3, 1988 [§ 13.46]

If the conflict-of-laws rules governing characterization of property interests are complicated when both spouses are domiciled in one jurisdiction, the difficulty is compounded in a dual-domicile marriage. The Act specifically states that, except as provided otherwise in chapter 766, the enactment of chapter 766 does not alter the classification and ownership rights of property acquired before the determination date. Wis. Stat. § 766.31(8). Before May 3, 1988, the determination date was defined as the last to occur of marriage, 12:01 a.m. on the date of establishment of a marital domicile in Wisconsin, or 12:01 a.m. on the effective date of chapter 766 (January 1, 1986). Wis. Stat. § 766.01(5) (1985–86). Unless a marital domicile were established in Wisconsin, there would be no determination date for the spouses, and the classification and ownership rights of their property would not be altered by the Act.

Before passage of the 1988 Trailer Bill, it was unclear what precisely was meant by the statutory phrase “a marital domicile in this state.” The Act did not define the term. The comment to UMPA section 1(5), on which section 766.01(5) is based, provided a clue. In relevant part it states the following:

The Act will apply to those *couples* now domiciled in an adopting state as well as those who move to one in the future. It will also apply to couples who marry in an adopting state after the Act is in effect. The definition of “determination date” creates a flexible formula to establish for individual *couples* in these three separate configurations the specific date as of which the Act is in effect with respect to their property....

(Emphasis added). Implicit in the words “those couples now domiciled” or “those [couples] who move” is that both spouses either are domiciled, or establish domicile, in the state adopting the Act.

The linkage of the adjective “marital” with “domicile” in section 766.01(5) (1985–86) (and elsewhere in the Act) before May 3, 1988 also cannot be ignored. The word “marital” implies being of the marriage, mutual choice, and a single location. The statute did not refer to

“establishment of domicile by a spouse” in Wisconsin or use any other configuration of words to intimate that the action of one spouse alone could trigger a determination date. Further, the Act was silent on the question whether one state or another would be the “deemed domicile” of choice when spouses reside in different states.

There was another view of the statutory language, however. This view held that if *either* spouse established a domicile in Wisconsin, then there must be a further inquiry as to whether that spouse intended to establish a marital domicile in this state. This view contended that the words “a marital domicile” may be synonymous with “the domicile of a spouse” if that spouse so intends. Proponents of this view argued that “*a* marital domicile” is not the same as “*the* marital domicile.” Thus, when spouses resided in two states, Wisconsin and state A, they may have intended to have a single marital domicile in Wisconsin, a single marital domicile in state A, or separate marital domiciles in the states in which each resided. The result rested purely on their intent. Under this analysis, when one spouse established residence in Wisconsin, further inquiry would be necessary to determine whether Wisconsin was intended to be the marital domicile of one or both spouses. If the requisite intent were established, then a determination date would be triggered for purposes of the Act. The difficulty, of course, is that if only one spouse intended to have a marital domicile in Wisconsin, applying the Act to the property or obligations of that spouse alone might produce strange results, although there is no public policy that appears to prohibit the Wisconsin domiciliary spouse from making that choice. Presumably the Act could not apply to the spouse who resides in state A and intends to have his or her domicile there.

At least three possible determination date scenarios could result, depending on the interpretation of the words “establishment of a marital domicile in this state.”

1. There is no determination date and the Act does not apply unless both spouses have or establish their domicile in Wisconsin. This interpretation of the statutory language seems to be the correct one, given the repeated use of the noun “couples” in the comment to UMPA section 1(5) and the use of the adjective “marital” to modify “domicile” in the statute itself.
2. There is a determination date and the Act applies to a spouse if that spouse has a domicile in Wisconsin. This alternative requires

interpreting the phrase “a marital domicile” as analogous to “the domicile of a spouse” if that spouse so intends. For reasons cited previously, this interpretation is not as persuasive as alternative 1 above. Adoption of this interpretation would subject the property of a spouse domiciled in Wisconsin to the Act, while the property of the nondomiciliary spouse would be subject to the property laws of the state where he or she resides. There would appear to be no obvious constitutional impediment to this view, however.

3. There is a determination date and the Act applies to both spouses even if only one spouse has a domicile in Wisconsin. In the case of a dual-domicile marriage, this interpretation would, in effect, make the Act a “long-arm” statute regarding the property of the nondomiciliary spouse and might not pass constitutional muster.

If alternative 1 is the appropriate rule for determining when the determination date occurs and the Act begins to apply, even more challenging problems exist for determining when it ceases to apply. No statute dealt with this subject; however, three additional scenarios can be envisaged:

4. The Act ceases to apply to both spouses as soon as one spouse is no longer domiciled in Wisconsin.
5. The Act ceases to apply to the property of one of the spouses when he or she establishes a domicile in a state other than Wisconsin, but it continues to apply to the property of the spouse who remains domiciled in Wisconsin.
6. The Act ceases to apply to the property of both spouses only when both spouses establish a domicile in a state other than Wisconsin.

If it is correct to conclude that the joint presence and intention of both spouses, that is, a mutual marital domicile as discussed in alternative 1, were required for a determination date to occur and the Act to apply, then it follows that when one or both spouses no longer have their domicile in Wisconsin, the Act would cease to apply to both. This interpretation is outlined in alternative 4. It appears constitutionally permissible for a court to adopt alternative 5 and determine that the Act applied to the property of a spouse who remains domiciled in Wisconsin after the other spouse established domicile in another jurisdiction, but such an interpretation is at odds with the determination date statute, which



seemingly required both spouses to be domiciled in the state. Alternative 6, like alternative 3, may have constitutional infirmities to the extent it attempts to extend the property laws of the state of Wisconsin to income or assets acquired by a spouse domiciled in another state.

The language of the statute itself and the comment to UMPA section 1(5) support alternative 1 as the correct interpretation of the pre-May 3, 1988 version of section 766.01(5) (1985–86) for determining when the Act begins to apply, and logic dictates that alternative 4 is the proper parallel rule for determining when the Act ceases to apply. Nevertheless, these rules might produce unintended results at the death of a Wisconsin domiciliary spouse in a dual-domicile marriage before May 3, 1988. The then-existing versions of deferred marital property election in section 861.02 (1985–86) and the election against the augmented marital property estate in section 861.03 (1985–86), involving probate and nonprobate property respectively, applied only “at the death of a spouse whose marital domicile is in this state.” As in section 766.01(5) (1985–86), the term *marital domicile* was not defined, although logically it should have the same meaning.

Assume that a married couple was domiciled in Iowa. After December 31, 1985, the husband moves to Wisconsin and commences employment and establishes domicile there. Meanwhile, the wife continues to live and work in Iowa. Assume further that this arrangement continues without the spouses obtaining a legal separation or divorce. The husband dies before May 3, 1988, leaving intangibles and real estate in Wisconsin. Clearly the husband is domiciled in Wisconsin for probate purposes. Because the husband has no “marital domicile” in Wisconsin under the rationale of alternative 1, neither the deferred marital property election statutes nor any other spousal election would be available to the wife with respect to the husband’s estate if he chose to disinherit her. (The Wisconsin probate court could order spousal or family allowances for the wife and minor children under sections 861.31–.35, however.)

The same problem could occur under alternative 4. Assume, for example, that both spouses were domiciled in Wisconsin. After December 31, 1985, the husband moves and establishes domicile in Iowa and is employed there, while the wife remains domiciled in Wisconsin. Under alternative 4, the Act would not apply to these spouses. If the wife died before May 3, 1988, neither spouse would have a “marital domicile” in Wisconsin. If the wife chose to disinherit her husband, the

deferred marital property elections of the versions of sections 861.02 and 861.03 then in effect would be unavailable, and the husband could not reach property in the hands of the decedent's personal representative or transferees that would have been marital property had both spouses continued their domicile in Wisconsin.

If the court adopted the view described in alternative 5, then the deceased Wisconsin spouse in the above example might be "a spouse whose marital domicile is in the state," and the deferred marital property election and the election against the augmented marital property estate might apply. However, the Wisconsin elective rights in all likelihood would not apply to the estate of the nondomiciliary spouse if he or she died first. Presumably, the Legislature did not contemplate these significant inconsistencies and problems with the definition of marital domicile during the formulation of the 1985 Trailer Bill.

### **b. After May 2, 1988 [§ 13.47]**

The basic rule set forth in section 766.03 is that the Act first applies to spouses on their determination date, defined in section 766.01(5)(b) as the date after January 1, 1986, on which both spouses are domiciled in Wisconsin. Thereafter, the Act continues to apply to the spouses "during marriage," defined in section 766.01(8) as the period during which both spouses are domiciled in Wisconsin, beginning with the determination date and ending either at dissolution of the marriage or at the death of a spouse. The Act will cease to apply when one of the spouses is no longer domiciled in Wisconsin. However, the fact that one of the spouses changes domicile by itself does not affect any property right, interest, or remedy acquired under the Act by either spouse or by a third party. Wis. Stat. § 766.03(3).

Because the law was uncertain before the adoption of these provisions, section 766.03(5) contains a saving provision to the effect that any property right, interest, or remedy that a spouse or third party acquired on or after January 1, 1986, and before May 3, 1988 (the effective date of the new provisions), as well as the property available to satisfy an obligation incurred during that period, is not adversely affected by the provisions.

In addition, subsections 766.61(3)(a)2. and (c)2. provide time-apportionment formulas for determining the marital property and

individual property components in certain life insurance policies when one spouse or both spouses become domiciled in another state. *See supra* §§ 2.168–.170.

A similar change in the formula for determining the marital property component in the deferred employment benefits of a spouse was adopted when section 766.62(1)(b) was amended by the 1988 Trailer Bill.

The 1988 Trailer Bill and 1998 Probate Code revision bill (1997 Wisconsin Act 188) also amended section 861.02 to make clear that a surviving spouse, regardless of domicile, may elect deferred marital property treatment of property owned by a spouse who dies domiciled in Wisconsin, including real property located in another jurisdiction.

## **2. General Rules Relating to Establishment of Domicile [§ 13.48]**

The general rules of law relating to the establishment of a domicile of choice have long been recognized in Wisconsin and elsewhere. Every person has a domicile at all times, and no person may have more than one domicile at a time, at least for the same purpose. Restatement § 11; *see also Eaton v. Eaton (In re Will of Eaton)*, 186 Wis. 124, 133, 202 N.W. 309 (1925). A domicile of choice requires the concurrence of physical presence in a place and an intention to make that place home. Restatement §§ 15, 16, 18; *see also Lauterjung v. Ford (In re Estate of Ford)*, 14 Wis. 2d 324, 327, 111 N.W.2d 77 (1961); *Rosick v. Morey (In re Estate of Morey)*, 272 Wis. 79, 82–83, 74 N.W.2d 823 (1956); *Will of Eaton*, 186 Wis. at 133. An established domicile of choice continues until it is superseded by the spouses establishing a new domicile. Restatement § 19. Early Wisconsin cases such as *Lauterjung* and *Eaton* required total abandonment of the prior domicile before acquisition of a new one, but this requirement has been dropped in more recent decisions. *Oak Park Trust & Savings Bank v. Tressing (In re Estate of Tressing)*, 86 Wis. 2d 502, 510, 273 N.W.2d 271 (1979); *Daniels v. Draves (In re Estate of Daniels)*, 53 Wis. 2d 611, 619, 193 N.W.2d 847 (1972).

The Wisconsin Supreme Court has held that when spouses live together but own two homes in different states and move back and forth between them, the domicile of choice of the spouses will be determined by intention, and physical acts will be evidence of which residence the parties consider their permanent home. *Tressing*, 86 Wis. 2d at 510;

*Daniels*, 53 Wis. 2d at 619. *Daniels*, however, made clear that this rule is limited to situations in which the spouses live together, and that the rule does not address situations in which spouses live apart by mutual consent in domiciles in different states for at least part of the time. *Daniels*, 53 Wis. 2d at 614. The general rule in the latter situation is that spouses living apart can acquire separate domiciles of choice. See Restatement § 21 cmt. d; *Green v. Commissioner of Corps. & Taxation*, 305 N.E.2d 92 (Mass. 1973).

The principles discussed above no doubt will be useful in determining whether a marital domicile has been established for purposes of the Act. Except in a minority of cases, it is unlikely that most married couples will formally express any intent concerning their marital domicile, with, for example, a written document or marriage agreement.

### 3. Dual Domicile Considerations [§ 13.49]

When spouses reside in different states, the same property interests may be characterized differently under the laws of the two states. This is most likely to pose problems at death or divorce; however, it might also create complications for Wisconsin income tax purposes if one spouse is not domiciled in Wisconsin for the entire tax year. See Wis. Stat. § 71.10(6)(d) (discussed at § 9.36, *supra*).

In the few cases to consider the issue, the courts have held that income and assets acquired with earnings are characterized according to the law of the jurisdiction where earned or acquired, even though the domicile of the spouses is elsewhere. *Mounsey v. Stahl*, 306 P.2d 258 (N.M. 1956), involved the characterization of a mineral interest located in New Mexico as community property or separate property. The spouses had their marital domicile in New York, and the husband conducted an oil and gas business with offices in New York and Texas. Absent a showing that the mineral interest in question was acquired with the husband's separate earnings generated in New York and not his community property earnings generated in Texas, the mineral interest was presumed under New Mexico law to be community property. See also *Trapp v. United States*, 177 F.2d 1 (10th Cir. 1949); *Hammonds v. Commissioner*, 106 F.2d 420 (10th Cir. 1939).

A second case, *Lane-Burslem v. Commissioner*, 659 F.2d 209 (D.C. Cir. 1981), involved spouses who claimed marital domicile in Louisiana

but resided and worked in England. The wife previously had been a Louisiana resident and intended to return there with her husband, a British citizen. The question was whether the wife could attribute one-half her earnings to her nonresident, alien husband as community income and thereby escape income tax on that portion. The court held that under the provisions of the Louisiana Civil Code then in effect, a nonresident spouse's community interest in the domiciliary spouse's property would be limited solely to property acquired in Louisiana. Applying a significant-relationship test, the court determined that the United Kingdom had the most significant relationship to the income; under English law, the income was the wife's separate property, not community property. And, in *Commissioner v. Cavanagh*, 125 F.2d 366 (9th Cir. 1942), in which the husband was domiciled in California and the wife in Canada, the court said that the husband was subject to income tax on only one-half his income because "the wife's interest in her husband's income [is] determined by the law of domicile where earned and not by the law of matrimonial domicile." *Id.* at 368.

However, in *Payne v. Commissioner*, 141 F.2d 398 (5th Cir. 1944), the court held that separate marital domiciles would not be recognized even if the spouses were separated. The wife resided and earned income in Texas, and the husband resided in Ohio. In determining that all the wife's Texas earnings were taxable to her, the court applied Texas conflict-of-laws rules that resolved the issue on the basis of marital domicile. Under the common law rule, marital domicile is the husband's place of residence, and thus the wife's earnings were characterized as separate property under Ohio law, rather than as community property under Texas law.

The above cases that look to the jurisdiction where income is earned appear to be consistent with the position taken in Restatement section 258, comment c, which states the following:

When the spouses have separate domicils at the time of the acquisition of the movable, the local law of the state where the spouse who acquired the movable was domiciled at the time will be applied, in the absence of an effective choice of laws by the parties, to determine the extent of the other spouse's marital interest therein.

On the other hand, the Court of Appeals of Arizona in *Martin v. Martin*, 752 P.2d 1026 (Ariz. Ct. App. 1986), *modified in part*, 752 P.2d 1038 (Ariz. 1988), cited reasons of judicial economy and uniformity of

result in applying its quasi-community property law to the assets of both parties, even though one spouse resided in California at the time of the divorce. A conflict-of-laws issue arose because the California spouse had significant postseparation earnings there. Such earnings are treated as the separate property of the earning spouse under California law, whereas they are treated as community property under Arizona law. In applying Arizona law to both parties, the court characterized the rule of Restatement section 258 as “anachronistic” and “unworkable in modern mobile America,” 752 P.2d at 1031 (citation omitted), because a trial court may find itself forced to apply various rules of state property law to different marital assets depending on where each spouse was domiciled when the particular asset was acquired. *See also Ismail v. Ismail*, 702 S.W.2d 216, 222 (Tex. App. 1985).

For further analysis of the complex issues involved when spouses have separate domiciles, see *Lintner, Marital Property Rights and Conflict of Laws When Spouses Reside in Different States*, 11 Comm. Prop. J. 283 (1984). In examining the various conflict-of-laws theories applicable to these problems, Lintner comments on the choice-influencing considerations approach followed in Wisconsin:

As applied to the rights of one spouse in the marital property of the other domiciled in a different state, the most relevant considerations would be predictability of results, simplification of the judicial task, and application of the “better rule of law”. As noted above, choosing one marital property system and applying it to all of the couple’s property would result in greater predictability and a simplification of the complex job of dividing up the couple’s property. Application of the “better rule of law” implies a subjective decision that could obstruct the goal of assuring predictable results. The consideration could be construed, however, to mean reaching the most equitable result.

*Id.* at 298.

The following example illustrates some of the potential property-related pitfalls of a dual-domicile marriage in which spouses are essentially estranged but not divorced.

➤ **Example.** The spouses maintain separate domiciles, the wife living in Wisconsin and the husband in Michigan. The husband owns real estate in Michigan, along with personal property investments titled in his name. All the personal property of the spouses was acquired from earnings after their marriage except for the Michigan

real estate, which was inherited. The husband dies. His will disinherits the wife.

What are the rights of the parties in this situation? The wife could file an election to take against the will under sections 700.2201–.2206 of the Michigan Statutes (current through P.A. 2010, No. 57, of the 2010 Regular Session, 95th Legislature) and thereby be entitled to a fractional share of the estate of the husband, including the Michigan real estate. The Michigan personal representative, by way of set-off, might seek to apply half the property titled in the wife's name against this statutory share on the ground that it represents the husband's share of Wisconsin marital property. Alternatively, the wife might ask the probate court in Michigan to determine that part of the husband's estate was marital property and to award her half. Again, half the assets in her name probably would be available to the personal representative as a set-off against any assets of the husband awarded to her. The Michigan courts would be most unlikely to entertain this action with respect to the Michigan real estate, because the real estate would not be treated as marital property even under Wisconsin law; they might also dismiss the action as to personal property accumulated by the husband while he was residing in Michigan.

Similar problems could occur if spouses decide to divorce after a lengthy separation during which they have accumulated property in two jurisdictions. If the other state has an equitable property-division statute similar to Wisconsin's, the fact that property is located in different jurisdictions and has different characteristics under the laws of each should not prove to be a major problem. It is likely that the difficulties that may occur at death will be avoided in a divorce because of the exclusion of inheritances and gifts from the divorce property division.

In the area of creditors' rights, the result may depend on where the suit is brought. Among the possible conflict-of-laws issues are the characterization of the spouses' mutual obligations of support, the existence of a doctrine of necessities, the characterization of the debt that was incurred, and the characterization of earnings and property acquired by the spouse domiciled in Wisconsin and by the spouse domiciled elsewhere for purposes of debt satisfaction. In these cases, it is likely that the grouping-of-contacts analytical framework of Restatement section 188 (discussed at section 13.6, *supra*) will be used to reach a decision. Nonetheless, the decision-making process will involve difficult issues. *See supra* § 13.17.

## H. Special Choice-of-laws Problems Involving Tort Causes of Action and Recoveries [§ 13.50]

In tort cases, Wisconsin follows the choice-influencing considerations approach of *Heath v. Zellmer*, 35 Wis. 2d 578, 151 N.W.2d 664 (1967) and concurrently applies the grouping-of-contacts approach of Restatement section 188 in contract cases. *Schlosser v. Allis-Chalmers Corp.*, 86 Wis. 2d 226, 271 N.W.2d 879 (1978); *see supra* §§ 13.4–.6. The multijurisdictional implications of personal injury cases pose some of the most difficult choice-of-laws questions. The residences of the plaintiff and defendant, the place where the injury occurred, the place where the conduct occurred, and the place where an insurance contract was written and delivered may all be in different states. In resolving which law to apply to various aspects of such a complex transaction, the courts in Wisconsin can be expected to use the approach outlined at sections 13.4–.6, *supra*.

A cause of action itself, however, is a species of property. In *Jaeger v. Jaeger*, 262 Wis. 14, 53 N.W.2d 740 (1952), the Wisconsin Supreme Court ruled that a wife's cause of action that accrued while the spouses were temporarily in Arizona was not classified as Arizona community property. The spouses were domiciled in Wisconsin and had an accident while traveling through Arizona. The wife sued her husband in Wisconsin for damages as the result of injuries sustained. In an apparent effort to bar the wife's suit against the husband, the defense was raised that the cause of action was community property. This theory assumed that damages become the community property of both spouses under Arizona law; that the husband has rights with respect to such property and must be a party to the suit; and that the husband's negligence is imputed to the wife, so that she cannot recover for injuries caused by that negligence. The court held that the law of the matrimonial domicile (Wisconsin) governed the characterization of the spouses' respective rights in the cause of action and that under Wisconsin law the cause of action was the wife's sole property.

Section 766.31(7)(f) deals with recoveries for personal injury and not causes of action as such. It creates a bifurcated treatment for such recoveries. The recovery is the individual property of the injured spouse, except for the portion attributable to expenses paid from marital property and amounts attributable to loss of income during marriage, which are marital property. Under *Jaeger*, the Wisconsin courts will no doubt



apply the statutory rules to recoveries received by spouses domiciled in Wisconsin from causes of action arising after the determination date in another state.

A more difficult question is how to determine the property-law classification of a cause of action that accrues to a spouse in another state after marriage but *before* the determination date, that is, before the spouses establish domicile in Wisconsin. Assume that the law of the other jurisdiction confers a vested property right in a cause of action solely in the injured party, including the right to recover lost income now and in the future. Because earnings are characterized as the sole property of the injured spouse under the laws of the other state, the classification of that part of the recovery as marital property under section 766.31(7)(f) conflicts with section 766.31(8), which purports to preserve the classification and ownership of predetermination date property. The former nonresident may cite *Jaeger v. Jaeger*, 262 Wis. 14, 53 N.W.2d 740 (1952), for the proposition that the law of the former marital domicile determines the classification of the cause of action. Once accrued, the cause of action and any recovery based on it are characterized as the solely owned property of the injured party under the laws of the former marital domicile. Section 766.31(8) recognizes that characterization. The attempted ex post facto classification of part of the *recovery* on the cause of action as marital property by section 766.31(7)(f) is thus problematic. The issue seems equally unclear with respect to causes of action that accrue before marriage to an injured party domiciled elsewhere who subsequently marries and moves to Wisconsin or who moves to Wisconsin and marries.

However, if an injured spouse dies after the spouses establish a marital domicile in Wisconsin, the augmented deferred marital property election of section 861.02 would apply to that portion of the recovery that would have been marital property if the recovery had occurred after the determination date. This follows because the portion of the recovery attributable to loss of income during marriage would have been marital property if the Act had applied to the spouses from the inception of their marriage.

**IV. Uniform Disposition of Community Property Rights at  
Death Act [§ 13.51]**

**UNIFORM DISPOSITION OF COMMUNITY  
PROPERTY RIGHTS AT DEATH ACT**

*Drafted by the*

NATIONAL CONFERENCE OF COMMISSIONERS ON  
UNIFORM STATE LAWS

*and by it*

APPROVED AND RECOMMENDED FOR ENACTMENT IN  
ALL THE STATES

*at its*

ANNUAL CONFERENCE  
MEETING IN ITS EIGHTIETH YEAR  
AT VAIL, COLORADO

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WITH  
PREFATORY NOTE AND COMMENTS

APPROVED BY THE AMERICAN BAR ASSOCIATION  
AT ITS MEETING AT NEW ORLEANS, LOUISIANA, FEBRUARY  
7, 1972

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UNIFORM STATE LAWS  
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UNIFORM DISPOSITION OF COMMUNITY PROPERTY  
RIGHTS AT DEATH ACT

#### PREFATORY NOTE

Frequently spouses, who have been domiciled in a jurisdiction which has a type of community property regime, move to a jurisdiction which has no such system of marital rights. As a matter of policy, and probably as a matter of constitutional law, the move should not be deemed (in and of itself) to deprive the spouses of any preexisting property rights. A common law state may, of course, prescribe the *dispositive* rights of its domiciliaries both as to personal property and real property located in the state. California's development of its "quasi-community property" laws illustrates the distinction.

The common law states, as contrasted to California, have not developed a statutory pattern for disposition of estates consisting of *both separate* property of spouses and property which was community property (or derived from community property) in which both spouses have an interest. In these states there have been relatively few reported cases (although the number has been increasing in recent years); the decisions to date show no consistent pattern and the increasing importance of the questions posed suggests the desirability of uniform

legislation to minimize potential litigation and to facilitate the planning of estates.

This Act has a very limited scope. If enacted by a common law state, it will only define the dispositive rights, at death, of a married person as to his interests at death in property “subject to the Act” and is limited to real property, located in the enacting state, and personal property of a person domiciled in the enacting state. The purpose of the Act is to preserve the rights of each spouse in property which was community property prior to change of domicile, as well as in property substituted therefor where the spouses have not indicated an intention to sever or alter their “community” rights. It thus follows the typical pattern of community property which permits the deceased spouse to dispose of “his half” of the community property, while confirming the title of the surviving spouse in “her half.”

It is intended to have no effect on the rights of creditors who became such before the death of a spouse; neither does it affect the rights of spouses or other persons prior to the death of a spouse. While problems may arise prior to the death of a spouse they are believed to be of relatively less importance than the delineation of dispositive rights (and the correlative effect on planning of estates). The prescription of uniform treatment in other contexts poses somewhat greater difficulties; thus this Act is designed solely to cover dispositive rights at death, as an initial step.

The key operative section of the Act is Section 3 which sets forth the dispositive rights in that property defined in Section 1, which is subject to the Act. Section 2 follows Section 1’s definition of covered property and is designed to provide aid, through a limited number of rebuttable presumptions, in determining whether property is subject to the Act.

No negative implications were intended to be raised by lack of inclusion of other presumptions in Section 2; areas not covered were simply left to the normal process of ascertainment of rights in property.

The first three sections form the heart of the Act; the succeeding sections might almost be described as precatory and have been added to clarify situations which would probably follow from the first three sections but which might raise questions. Thus, Section 8 makes it clear that nothing in the Act prevents the spouses from severing any interest in community property or creating any other form of ownership of property

during their joint lives; and, such action on their part will effectively remove any property from classification as property subject to this Act. Similarly, Section 9 makes it clear that the Act confers no rights upon a spouse where, by virtue of the property interests existing during the joint lives of the spouses, that spouse had no right to dispose of such property at death. By way of illustration, in at least one community property jurisdiction, the wife has no right to dispose of any part of the community property if she predeceases her husband. If the law of that jurisdiction is construed so as to treat this as a rule of property, then the move to the common law state should not alter the “property interest” of the spouses by conferring a right on the wife which she did not previously possess. On the other hand, if the provision is treated as simply establishing a pattern of dispositive rights on death of a wife who predeceases her husband, rather than a property right, the common law state of new domicile could prescribe an alternative pattern of dispositive rights. The Act does not resolve this question; rather it simply makes clear that it does not affect existing “property rights,” leaving to the courts the interpretation of the effect of the community property state’s law.

#### UNIFORM DISPOSITION OF COMMUNITY PROPERTY RIGHTS AT DEATH ACT

SECTION 1. [*Application.*] This Act applies to the disposition at death of the following property acquired by a married person:

- (1) all personal property, wherever situated:
  - (i) which was acquired as or became, and remained, community property under the laws of another jurisdiction; or,
  - (ii) all or the proportionate part of that property acquired with the rents, issues, or income of, or the proceeds from, or in exchange for, that community property; or
  - (iii) traceable to that community property;
- (2) all or the proportionate part of any real property situated in this state which was acquired with the rents, issues or income of, the proceeds from, or in exchange for, property acquired as or which became, and remained, community property under the laws of another jurisdiction, or property traceable to that community property.

#### COMMENT

This section defines property subject to the Act.

**Subsection (1): Personal Property**

Subsection (1) is designed to cover all personal property which was acquired while the spouses were domiciled in a community property state, to the extent that it would have been treated as community property by that state at the time of acquisition and that no further action terminated the community character of the property. It also includes any property which was not originally community property but became such by agreement and, further, brings within the Act any personal property which can be traced back to a community source. Again, the Act only applies if there was no severance of the community interests [Section 8]. [While Section 3 applies to the dispositive rights of persons domiciled in the enacting state, the Act, as a practical matter, may be effective as to property located outside the state only to the extent that the state of the situs of the property is willing to recognize the policy of the domiciliary state.]

➤ *Example 1.* H and W, while domiciled in California, purchased 100 shares each of A Co., B Co. and C Co. stock with community property (earnings of H). H and W were transferred to a common law state which had not enacted this Act; while domiciled there H sold the 100 shares of A stock and with the proceeds purchased 100 shares of D stock. Subsequently H and W became domiciled in Michigan which had enacted this Act; H sold the B stock and 50 shares of D Co. stock and purchased 150 shares of E stock. H died domiciled in Michigan with 100 shares of C Co., 50 shares of D Co. and 150 shares of E Co. stock; all of the stock had always been registered in H's name. All of the shares, traceable to community property or the proceeds therefrom, constitute property subject to this Act.

**Subsection (2): Real Property**

Subsection (2) deals with real property and is confined to real property located within the enacting state (since presumably the law of the situs of the property will govern dispositive rights). The policy and operation of this subsection are intended to be the same as those set forth in subsection (1).

➤ *Example 2.* H and W, while domiciled in California, purchased a residence in California. They retained the residence in California when they were transferred to Wisconsin. After becoming domiciled

in Wisconsin they used community funds, drawn from a bank account in California, to purchase a Wisconsin cottage. H and W subsequently became domiciled in Michigan; they then purchased a condominium in Michigan for \$20,000 using \$15,000 of community property funds drawn from their bank account in California and \$5,000 earned by H after the move to Michigan. H died domiciled in Michigan; title to all of the real property was in H's name. Assuming Michigan had enacted this Act, three-fourths of the Michigan condominium would be property subject to this Act; the Michigan statute would not, however, apply to either the Wisconsin or California real estate. If Wisconsin had enacted this Act, the Wisconsin statute would apply to the Wisconsin cottage.

### **Subsections (1) and (2): Apportionment**

In both subsections (1) and (2) an apportionment is required by the phrase "all or the proportionate part" where personal property, or real property situated in the enacting state, has been acquired partly with property described as subject to the Act and partly with other (separate) property. To put it succinctly, the phrase represents a condensation of an area covered by many pages in a prior draft and is simply a statement of policy; it leaves to the courts the difficult task of working out the precise interest which will be treated as the "proportionate part" of the property subject to the dispositive formula of Section 3. Simply by way of illustration, assume that a single man (domiciled in a community property state) purchased a life insurance policy with a face amount of \$100,000 and an annual premium of \$1,000. Assume further that he paid three premiums and then entered into marriage. Further assume that the next seven premiums were paid with his earnings while domiciled in the community property state and that he and his wife then moved to a common law state where the next ten premiums were paid from his earnings in that common law state; he then died after the payment of the twenty premiums. Under one interpretation of the law of Texas the contract would remain the separate property of the insured; the community would have a claim for community funds advanced to pay premiums and, ignoring interest, it would appear that \$7,000 of the proceeds would be treated as community property and the remaining \$93,000 would be treated as the separate property of the deceased spouse. On the other hand, a state like California would probably treat the proceeds as being 65% separate and 35% community (basing the allocation of proceeds upon the percentage of separate and community funds contributed). Further variations could be mentioned. The

illustration is one of the simpler problems. Much more difficult problems are encountered where benefits under a qualified pension and profit-sharing plan are involved and the employee has been domiciled in both community property and common law jurisdictions during the period in which benefits have accrued. Attempts at defining the various types of situations which could arise and the varying approaches which could be taken, depending upon the state, suggest that the matter simply be left to court decision as to what portion would, under applicable choice of law rules, be treated as community property. The principle suggested is that at least a portion should be treated as community, if the appropriate law so treated it. Ordinarily, such questions should not arise if the problem is foreseen and effective planning takes place prior to death of a spouse.

SECTION 2. [*Rebuttable Presumptions.*] In determining whether this Act applies to specific property the following rebuttable presumptions apply:

(1) property acquired during marriage by a spouse of that marriage while domiciled in a jurisdiction under whose laws property could then be acquired as community property is presumed to have been acquired as or to have become, and remained, property to which this Act applies; and

(2) real property situated in this State and personal property wherever situated acquired by a married person while domiciled in a jurisdiction under whose laws property could not then be acquired as community property, title to which was taken in a form which created rights of survivorship, is presumed not to be property to which this Act applies.

#### COMMENT

The purposes of the rebuttable presumptions are simply to assist a court in applying the definitions in Section 1, through a process of tracing the property to a community property origin.

#### Subsection (1)

Subsection (1) of Section 2 deals with property acquired by the spouses while domiciled in a community property state. It thus provides that if one of the spouses acquired property while so domiciled, such property is “presumed” (a rebuttable presumption) to have been and remained community. It may be shown, of course, that such property was the separate property of the spouse and the law of the state of domicile may furnish the rule. For example the law of community



domicile may provide the rule that property acquired in the name of the wife shall be deemed to be her separate property or that a particular subsequent act effectively severed the community property interests.

➤ **Example 1.** H, married to W and domiciled in California, acquired stock; later H and W became domiciled in Michigan. Such property, if retained, is presumed to be property subject to this Act. By operation of Section 1 the proceeds of sale or exchange of such stock, and property acquired with the proceeds or income of such stock, would be deemed subject to the Act. If, however, upon the death of H, H's personal representative rebutted the presumption by evidence that the stock was acquired by H with his separate property (or by inheritance) neither the stock nor property acquired with that property or the income therefrom (unless the income itself would be subject to the Act because, under the applicable law, income from separate property is deemed to be community property) would be subject to this Act. Similarly the presumption may be rebutted by showing that such property, though originally community property, was effectively severed by an act of the spouses. It should be emphasized that the presumption is simply one of procedural convenience and neither changes the nature of the property interests nor prevents an interested person from showing the separate nature of the property.

### **Subsection (2)**

Subsection (2) sets up a rebuttable presumption that where a domiciliary of a *common law* state acquired property in such form as to indicate that title was in joint tenancy, tenancy by the entireties, or some other form of joint ownership with right of survivorship, it will be presumed that the property is not subject to the Act. This presumption was deemed appropriate as expressing the normal expectations of the spouses and to facilitate ascertainment of title to real property located in the enacting state, as well as personal property wherever located.

➤ **Example 2.** John and Mary Jones, formerly domiciled in California, became domiciled in Illinois and purchased a residence, taking title in the names of "John and Mary Jones as joint tenants, and not as tenants in common, with right of survivorship." Regardless of the source of the funds, the Illinois residence would be presumed to be held in joint tenancy and not subject to this Act.

SECTION 3. [*Disposition upon Death.*] Upon death of a married person, one-half of the property to which this Act applies is the property of the surviving spouse and is not subject to testamentary disposition by the decedent or distribution under the laws of succession of this State.

One-half of that property is the property of the decedent and is subject to testamentary disposition or distribution under the laws of succession of this State. With respect to property to which this Act applies, the one-half of the property which is the property of the decedent is not subject to the surviving spouse's right to elect against the will [and no estate of dower or curtesy exists in the property of the decedent].

#### COMMENT

This section deals with the dispositive rights, at death, of (1) a married person domiciled in the enacting state as to personal property and (2) of any married person, including a nondomiciliary of the enacting state, as to real property located in the enacting state; it also sets forth rules for intestate succession to property subject to this Act.

#### Testate Disposition

The dispositive pattern is the usual one encountered in the community property states; the deceased spouse may dispose of his one-half of the community property, subject to the provisions of Section 9.

➤ **Example.** H and W were formerly domiciled in California and are now domiciled in Michigan. All of their property was community property prior to the move from California to Michigan. At H's death he held title to a home in Michigan which had been purchased with the proceeds of the sale of a home in California which had been community property. Stock acquired as community property in California was held in his name in safety deposit boxes located in Illinois and Michigan. H and W had acquired a cottage in California as community property, held in H's name, and it was so held at the time of his death. H and W acquired a Michigan resort condominium, taking title as tenants by the entireties. H acquired bonds issued by his employer with earnings in Michigan and held title in his own name.

The Michigan residence and the stock would be deemed property subject to this Act and H would have the right under Section 3 to dispose

of half of that property by his will. The remaining property would not be deemed subject to this Act.

### **Intestate Succession**

If the property subject to this Act passes by intestate succession, the law of the enacting state applies to the decedent's one-half, again subject to Section 9. If under the law of the enacting state, a surviving spouse is entitled to one-third of the decedent's property by intestate succession, the result of the Act is to give to her two-thirds of the property subject to the Act. For example, if the spouses had recently moved to a common law state and owned \$300,000 of property (all being personal property held in the husband's name and acquired as community property), the wife would be entitled to one-half of the property (\$150,000) and would receive a 1/3 share of the husband's half (\$50,000) for a total of \$200,000. It is clearly within the power of the enacting state to prescribe any pattern of intestate succession deemed appropriate, and views may differ. In some community property states, the surviving spouse receives all of the decedent's community property upon intestate succession; in another, she would receive none. Similarly, the common law state may alter the pattern to fit its own policy determination.

### **Dower, Curtesy, Elective Share**

Dower and curtesy do not exist in community property and have been abolished in many common law states; policy considerations suggest that no such interest should exist in property subject to this Act, since the surviving spouse already has a one-half interest in such property. Similar reasons suggest a denial of any right in the surviving spouse to elect a statutory share in the one-half of the property over which the decedent had a power of disposition.

SECTION 4. [*Perfection of Title of Surviving Spouse.*] If the title to any property to which this Act applies was held by the decedent at the time of death, title of the surviving spouse maybe perfected by an order of the [court] or by execution of an instrument by the personal representative or the heirs or devisees of the decedent with the approval of the [court]. Neither the personal representative nor the court in which the decedent's estate is being administered has a duty to discover or attempt to discover whether property held by the decedent is property to which this Act applies, unless a written demand is made by the surviving spouse or the spouse's successor in interest.

## COMMENT

This section simply provides for perfection of title interests of the surviving spouse (e.g. where title was in the name of the deceased spouse) by orders of the court of appropriate jurisdiction (e.g. the probate court) in the enacting state. This section is designed to eliminate any liability of the personal representative for a breach of his fiduciary duty by failing to search for or to discover whether property held by the decedent is property defined in Section 1, unless a written demand is made by the surviving spouse or the spouse's successor in interest. In several states the Court administering a decedent's estate has a duty or undertakes to advise parties in interest of their legal and equitable rights, and this section is similarly designed to eliminate such Court's liability for failing to discover the community rights and to advise the interested party of his rights. Nothing contained in this section is to be construed to interfere with the Court's jurisdiction in a proper proceeding to perfect the title of the surviving spouse in and to property to which this Act applies.

SECTION 5. [*Perfection of Title of Personal Representative, Heir or Devisee.*] If the title to any property to which this Act applies is held by the surviving spouse at the time of the decedent's death, the personal representative or an heir or devisee of the decedent may institute an action to perfect title to the property. The personal representative has no fiduciary duty to discover or attempt to discover whether any property held by the surviving spouse is property to which this Act applies, unless a written demand is made by an heir, devisee, or creditor of the decedent.

## COMMENT

This section is a corollary to Section 4. Since title is apparently in the surviving spouse, the section simply provides for an action by the personal representative, heirs, or devisees and is again designed to eliminate any liability of the personal representative for a breach of his fiduciary duty by failing to discover or to attempt to discover whether property held by the surviving spouse is property subject to this Act, absent a written demand by an heir, devisee or creditor of the decedent.

SECTION 6. [*Purchaser for Value or Lender.*](a) If a surviving spouse has apparent title to property to which this Act applies, a purchaser for value or a lender taking a security interest in the property

takes his interest in the property free of any rights of the personal representative or an heir or devisee of the decedent.

(b) If a personal representative or an heir or devisee of the decedent has apparent title to property to which this Act applies, a purchaser for value or a lender taking a security interest in the property takes his interest in the property free of any rights of the surviving spouse.

(c) A purchaser for value or a lender need not inquire whether a vendor or borrower acted properly.

(d) The proceeds of a sale or creation of a security interest shall be treated in the same manner as the property transferred to the purchaser for value or a lender.

#### COMMENT

This section is designed to protect purchasers and lenders taking a security interest, who acquire such interest for value, after the death of the decedent, from a person who appears to have title to property to which this Act applies. The only requirement is that the purchaser or lender have acquired his interest for value; there is no requirement of good faith absence of notice. The purpose of the section is to permit reliance upon apparent title and facilitate both ascertainment of title and disposition of assets where adequate consideration is paid. Since, during the joint lives of the spouses, the spouse with apparent title would have been able to convey title (at least as to community property) though being held accountable to the other spouse for an appropriate allocation of the proceeds or any breach of fiduciary obligation, the Act simply extends this treatment to disposition of the assets after the death of a spouse.

SECTION 7. [*Creditor's Rights.*] This Act does not affect rights of creditors with respect to property to which this Act applies.

SECTION 8. [*Acts of Married Persons.*] This Act does not prevent married persons from severing or altering their interests in property to which this Act applies.

#### COMMENT

The rights, and procedures, with respect to severance of community property vary markedly among the community property states. The Act simply makes clear that nothing in the Act itself in any way limits the

rights of the spouses to sever community property or to create a form of ownership not subject to this Act.

SECTION 9. [*Limitations on Testamentary Disposition.*] This Act does not authorize a person to dispose of property by will if it is held under limitations imposed by law preventing testamentary disposition by that person.

SECTION 10. [*Uniformity of Application and Construction.*] This Act shall be so applied and construed as to effectuate its general purpose to make uniform the law with respect to the subject of this Act among those states which enact it.

SECTION 11. [*Short Title.*] This Act may be cited as the Uniform Disposition of Community Property Rights at Death Act.

SECTION 12. [*Repeal and Effective Date.*] The following acts and laws are repealed as of the effective date of this Act:

(1)

(2)

SECTION 13. [*Time of Taking Effect.*] This Act shall take effect....

# 14

## Ethical Considerations

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As a result of circumstances beyond the publisher's control, the revision of chapter 14 has been delayed. What follows is the chapter and supplement as it appeared in the previous edition. The State Bar of Wisconsin will provide, at no additional charge, the revised chapter to all book owners when it becomes available. If you have any questions, please contact the State Bar at 800-728-7788.





## Ethical Considerations

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## I. [§ 14.1] Scope of Chapter

This chapter addresses the factors that a lawyer should consider when deciding whether the joint representation of spouses is appropriate and ethical in various situations, including estate planning, drafting marital property agreements, advising spouses in credit transactions, probate, and divorce. The chapter also includes sample letters advising spouses of possible conflicts of interest when a lawyer represents both of them jointly.

This chapter approaches its topic by first laying out the basic policy issues underlying the ethical rules applicable in the marital property context and suggesting various factors relevant to the application of those rules (see sections 14.2–.5, *infra*). Next, the chapter examines the ethics rules of

primary importance in marital property law (see sections 14.6–.14, *infra*) and then switches focus to the aspects of marital property law of primary importance in an analysis of the ethics of joint representation (see sections 14.15–.23, *infra*). Next the chapter reviews common examples of the interaction of ethics law with marital property law (see sections 14.24–.34, *infra*). Finally, the chapter provides some sample engagement letters (see sections 14.35–.36, *infra*).

## **II. [§ 14.2] General Approach to Representing One or Both Spouses**

### **A. [§ 14.3] General Considerations**

Advising spouses who live under a community property regime such as the one established by the Wisconsin Marital Property Act<sup>1</sup> requires a lawyer to be alert to more and often different ethical concerns than does advising spouses who live under a common law regime. The primary source of the additional ethical concerns is the nature of community property (or Wisconsin marital property) itself. *See infra* § 14.15.

The ethical problems raised by the Wisconsin Marital Property Act primarily involve the following: (1) each spouse's right and need to have independent legal advice, and the lawyer's corresponding duty of undivided loyalty without conflicts of interest; (2) a spouse's interest in consulting freely and confidentially with his or her lawyer, and the lawyer's corresponding duty to preserve client confidences; and (3) a lawyer's need to promote client and public confidence in the integrity of the legal system and to avoid the appearance of impropriety. *See infra* § 14.14.

Any consideration of the professional ethics involved in serving clients relative to marital property must be based first on an understanding of the relevant provisions of the Rules of Professional Conduct for Attorneys and

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<sup>1</sup> 1983 Wis. Act 186 [hereinafter the Act or the Wisconsin Marital Property Act], *reprinted infra* the Appendix. The bulk of the Wisconsin Marital Property Act is codified as amended at chapter 766 of the Wisconsin Statutes, *reprinted infra* the Appendix. Textual references to the Wisconsin Statutes are hereinafter indicated as 'chapter xxx' or 'section xxx.xx,' without the designation "of the Wisconsin Statutes." Unless otherwise indicated, all references to the Wisconsin Statutes are to the 2001–02 Wisconsin Statutes, as affected by acts through 2003 Wisconsin Act 38.

their application. Wisconsin has adopted,<sup>2</sup> with some modifications, the American Bar Association Model Rules of Professional Conduct,<sup>3</sup> effective January 1, 1988. The Rules of Professional Conduct for Attorneys adopted in Wisconsin constitute chapter 20 of the Wisconsin Supreme Court Rules.<sup>4</sup>

Whether one lawyer may represent both spouses (or, more generally, more than one person) in estate planning, estate and trust administration, and related matters has received the attention of interested professional groups, among them the Special Study Committee on Professional Responsibility of the ABA Section of Real Property, Probate and Trust Law and the American College of Trust and Estate Counsel.<sup>5</sup> Members of these groups, among others, have asserted that the applicable ethical rules should permit a lawyer, when not acting as an advocate, to act in a joint representation capacity in advising spouses in estate planning and similar circumstances. Further, some members have asserted that the ABA Model Rules of Professional Conduct (especially the conflict-of-interest rules) do not adequately address clients' needs and interests in these situations.<sup>6</sup>

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<sup>2</sup> Wis. Sup. Ct. Order, June 10, 1987, 139 Wis. 2d xiii (1987) [hereinafter "Rules of Professional Conduct for Attorneys"].

<sup>3</sup> Model Rules of Professional Conduct (1983) [hereinafter ABA model rules or model rules].

<sup>4</sup> Rules of Professional Conduct for Attorneys, SCR ch. 20 (1988) [references to individual rules are hereinafter indicated as SCR 20:x.x].

<sup>5</sup> Am. Bar Ass'n, *Comments and Recommendations on the Lawyer's Duties in Representing Husband and Wife*, reprinted in 28 Real Prop. Prob. & Tr. J. 765 (Winter 1994) [hereinafter *Representing Husband and Wife*]; *ACTEC Commentaries*, *infra*, note 10; see also *Developments Regarding the Professional Responsibility of the Estate Planning Lawyer: The Effect of the Model Rules of Professional Conduct*, 22 Real Prop. Prob. & Tr. J. 1 (1987) [hereinafter *Developments*] (regarding American Bar Association); Jackson M. Bruce, Jr., *Ethics in Estate Planning and Estate Administration*, 15 Prob. Notes 118 (1989) (published by the American College of Probate Counsel, now American College of Trust and Estate Counsel).

<sup>6</sup> See *infra* § 14.4 (quoting introduction to third edition of the ACTEC Commentaries, *supra* note 10). For further discussion regarding the application of the ABA Model Rules of Professional Conduct in the estate planning context, see John R. Price, *Ethics in Action, Not Ethics Inaction: The ACTEC Commentaries on the Model Rules of Professional Conduct*, 29 *The Annual Phillip E. Heckerling Institute on Estate Planning* ch. 7 (1995); Jeffrey N. Pennell, *Ethics, Professionalism and Malpractice Issues in Estate Planning and Administration*, C126

## B. [§ 14.4] Independent, Joint and Separate Representation

It will be useful to distinguish three potential modes of representing spouses with respect to their property interests. As used in this chapter:

- *Independent representation* refers to the representation of husband and wife independently, by different lawyers.
- *Joint representation* (sometimes called *dual representation*) refers to the common representation of husband and wife as joint (as opposed to separate) clients.
- *Separate representation* refers to the common representation of husband and wife as separate clients of the same attorney. As discussed below, separate representation is problematic and unusual.

1. *Independent Representation.* The “easy solution” to a number of the ethical concerns involving marital property is simply to avoid them by requiring that each spouse obtain independent legal advice. This solution requires at least one additional attorney and sometimes two additional attorneys, if the attorney who originally represented one or both of the spouses can no longer ethically serve them. Independent representation also eliminates most, if not all, of the ethical issues unique to marital property law. However, the easy solution may be unwise, as well as inefficient, for a number of reasons: higher costs, increased complications and delays, and possibly more disputes. In fact, the New York Court of Appeals has stated that, in appropriate cases, the parties have an “absolute

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ALI-ABA 67 (June 18, 1995); Randall W. Roth, *Current Ethical Problems in Estate Planning*, C992 ALI-ABA 439 (Feb. 23, 1995); Bruce S. Ross, *How to Do Right by Not Doing Wrong: Legal Malpractice and Ethical Considerations in Estate Planning and Administration*, 28 *The Annual Phillip E. Heckerling Institute on Estate Planning* ch. 8 (1994); Russell G. Pearce, *Family Values and Legal Ethics: Competing Approaches to Conflicts in Representing Spouses*, 62 *Fordham L. Rev.* 1253 (1994); Louis A. Mezzullo, *Ethics for Estate Planners*, C960 ALI-ABA 65 (Oct. 26, 1994); Robert L. Manley, *The Impact of Ethical Rules on Estate Planning*, C966 ALI-ABA 371 (July 22, 1994); Hazard, *supra* note 13; Geoffrey C. Hazard, Jr. & W. William Hodes, *The Law of Lawyering: A Handbook on the Model Rules of Professional Conduct* (1993); Jeffrey N. Pennell, *Professional Responsibility: Reforms Are Needed to Accommodate Estate Planning and Family Counselling*, 25 *The Annual Phillip E. Heckerling Institute on Estate Planning* ch. 18 (1991), (especially paragraph 1803); Gerald P. Johnston, *Avoiding Malpractice Liability in the Estate Planning Context*, U. S. Cal. 1991 Inst. on Fed. Tax., ch. 17 (1991) (especially section 1705).

right” to be represented by the same attorney. *Levine v. Levine*, 436 N.E.2d 476, 479 (N.Y. 1982).

2. *Joint Representation.* The principles of legal ethics recognize the efficacy of joint representation in proper cases. As one commentator has written, “There are, however, not infrequently cases in which it is highly desirable and to the advantage of everyone concerned that the same lawyer should, at the desire of both parties, represent them both.”<sup>7</sup>

When independent representation is unnecessarily recommended or insisted on by an attorney, the public may be justified in concluding that the lawyers are making matters more complicated than necessary and “feathering their own nests.” Such a perception hardly promotes public confidence in the integrity of the legal system and the efficiency of the legal profession.<sup>8</sup>

In addition, the independent representation solution may be contrary to the bar’s arguable duty to make legal services available to the public at a reasonable cost.<sup>9</sup> An attorney’s ethical responsibilities to his or her client include the duty to provide services and representation competently, efficiently, and economically.

The trend in the law governing lawyers seems to support the position of this chapter that efficiency and economy remain proper considerations in rendering legal services and are relevant to ethical considerations, if in the client’s (or clients’) best interest(s). Supreme Court Rule 20:2.2 recognizes the propriety of a lawyer serving as an “intermediary” when the lawyer believes that the matter can be resolved on terms compatible with the clients’ best interests and that each client can make adequately informed

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<sup>7</sup> Henry S. Drinker, *Legal Ethics* 120 (1953).

<sup>8</sup> See former SCR 20.48(2) (EC 9 2) (lawyer’s duty to promote “public confidence in the integrity and efficiency of the legal system and the legal profession”). See *infra* 18, *infra* § 14.14 for a discussion of the continued relevance of the ABA Code.

<sup>9</sup> Former SCR 20.06 (canon 2) (which provided that a lawyer should assist the legal profession in fulfilling its duty to make legal counsel available) and former SCR 20.12 (DR 2 106) spoke in terms of reasonable compensation. The clear import is that efficiency in rendering services and obtaining results has been an appropriate ethical consideration. See Keith Kaap, *Ethics and Professional Responsibility: A Handbook for Wisconsin Lawyers* 2-105 (State Bar of Wisconsin CLE Books 1986 & Supp.) (out of print). See *infra* note 18.

decisions, and when each client provides informed consent to the common representation. *See infra* § 14.11.

The efficacy of multiple representation in the context of trusts and estates practice is one of the main themes of the *ACTEC Commentaries on the Model Rules of Professional Conduct*, originally approved by the Board of Regents of the American College of Trust and Estate Counsel in October 1993 and now in their third edition.<sup>10</sup>

On the subject of multiple representation, the ACTEC Commentary on Model Rule 1.7 (Conflict of Interest: General Rule) emphasizes that in many instances, it may be appropriate for a lawyer to represent more than one member of the same family in connection with each person's estate plan. The commentary notes that in some instances the clients may actually be better served by such a representation, resulting in more economical and better coordinated estate plans.

3. *Separate Representation.* The ACTEC Commentary on Model Rule 1.7 also addresses the possibility of separate representation (a lawyer simultaneously representing both husband and wife as separate, as opposed to joint, clients), acknowledging that this mode of representation has received criticism. The Commentary provides the following example:

Example 1.7-1. Lawyer (*L*) was asked to represent Husband (*H*) and Wife (*W*) in connection with estate planning matters. *L* had previously not represented

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<sup>10</sup> Am. Coll. of Trust & Estate Counsel, *ACTEC Commentaries on the Model Rules of Professional Conduct* (3d ed. 1999) [hereinafter *ACTEC Commentaries*]. The Commentaries are available in print from ACTEC and also online at ACTEC's Web site, [www.actec.org](http://www.actec.org). As of the date of publication the precise link is <http://www.actec.org/pubInfoArk/comm/toc.html>. The Commentaries represent an effort by ACTEC to provide "particularized guidance" to lawyers, courts, and ethics committees regarding trusts and estates lawyers' professional responsibility. The Commentaries are intended to provide assistance in interpreting the model rules and eventually developing amendments to them. The Commentaries do not, however, constitute an official interpretation of the model rules. The introduction to the third edition summarizes the purpose of the Commentaries as follows: "Neither the Model Rules of Professional Conduct (MRPC) nor the Comments to them provide sufficiently explicit guidance regarding the professional responsibilities of lawyers engaged in a trusts and estates practice. Recognizing the need to fill this gap, ACTEC has developed the following Commentaries on selected rules to provide some particularized guidance to ACTEC Fellows and others regarding their professional responsibilities."

either *H* or *W*. At the outset *L* should discuss with *H* and *W* the terms upon which *L* would represent them. Many lawyers believe that it is only appropriate to represent a husband and wife as joint clients, between whom the lawyer could not maintain the confidentiality of any information relevant to the representation. However, some experienced estate planners believe that it is appropriate to represent a husband and wife as separate clients, each of whom is entitled to presume the confidentiality of information disclosed to the lawyer in connection with the representation. If permitted by the jurisdiction in which the lawyer practices, the lawyer may properly represent a husband and wife as separate clients. Whether the lawyer represents the husband and wife jointly or separately, the lawyer should do so only with their consent after disclosure of the implications of doing so. The same requirements apply to the representation of others as joint or separate multiple clients, such as the representation of other family members, business associates, etc.<sup>11</sup>

The separate representation of both spouses as clients is explored in greater detail in *Representing Husband and Wife*, a report of the Special Study Committee on Professional Responsibility of the Section of Real Property, Probate and Trust Law of the American Bar Association. See *supra* note 5. The report discusses ethical considerations under the ABA model rules involved in selecting the mode of representing spouses, the duties and obligations that arise under various scenarios depending on the mode of representation selected, and the duties and obligations applicable in the absence of an agreement with the spouses regarding the mode of representation.<sup>12</sup>

Some commentators are critical of the practice of separately representing spouses. For example, Professor Geoffrey C. Hazard, Jr., describes the

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<sup>11</sup> *ACTEC Commentaries*, *supra* note 10. For a summary of the purpose and some of the major contributions of the *ACTEC Commentaries*, see Bruce S. Ross, 'Particularized Guidance' for the Estate and Trust Lawyer, 133 Tr. & Est. 10 (July 1994). The *ACTEC Commentaries* are discussed in greater depth in John R. Price, *Ethics in Action, Not Ethics Inaction: The ACTEC Commentaries on the Model Rules of Professional Conduct*, 29 *The Annual Phillip E. Heckerling Institute on Estate Planning* ch. 7 (1995).

<sup>12</sup> For a discussion of the report, see Malcolm A. Moore & Anne K. Hilker, *Representing Both Spouses: The New Section Recommendations*, 7 Prob. & Prop. 26 (July/Aug. 1993); Russell G. Pearce, *Family Values and Legal Ethics: Competing Approaches to Conflicts in Representing Spouses*, 62 Fordham L. Rev. 1253 (1994); *Report of Working Group on Spousal Conflicts*, 62 Fordham L. Rev. 1027 (1994) (from the December 3–5, 1993, Fordham University School of Law Conference on Ethical Issues in Representing Older Clients).



concept of separate representation as “a legal and ethical oxymoron,” and “incorrect as a matter of law and therefore a legally dangerous mode of practice.”<sup>13</sup>

### **C. [§ 14.5] Suggested Factors for Determining Independent or Joint Representation**

The rules governing professional conduct often do not give clear-cut answers. There may be a dearth of guidance, and only a few ethics opinions may be found on the subjects involved.<sup>14</sup> The State Bar of Wisconsin Standing Committee on Professional Ethics Formal Opinion E-89-10 (1989) lists the factors to consider in determining whether joint representation as an intermediary is appropriate under SCR 20:2.2. *See infra* note 21. While helpful, that opinion addressed a proposed business representation.

The bias of this chapter is toward efficiency and economy, consistent with proper ethical standards, with the clients’ interests being the paramount consideration. The factors listed below are relevant in applying the Rules of Professional Conduct for Attorneys to the ethical concerns raised by the marital property system in Wisconsin.

Determining the proper response to the ethical concerns connected with marital property involves weighing a client’s interest in receiving sound, independent professional advice and judgment on the one hand, and the client’s interest in efficient, economical legal advice and assistance on the other. *See Developments in the Law: Conflicts of Interest in the Legal Profession*, 94 Harv. L. Rev. 1244, 1309–11 (1981). An analysis of the model rules, case authority, ethics opinions, and other supporting authority indicates that an attorney should consider the following factors in an attempt to strike a balance between these two interests.

1. *Ethical judgment*—whether a clear answer to the ethical question involved is evident, or whether there are well-supported differences of ethical opinion. If a clear answer is evident or if the matter is governed by a rule of professional conduct, the answer or rule governs. On the

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<sup>13</sup> Geoffrey C. Hazard, Jr., *Conflict of Interest in Estate Planning for Husband and Wife*, 20 Prob. Law. 1, 5–6, 11–15 (Summer 1994).

<sup>14</sup> *See Kaap, supra* note 9, at 1–4; *see also* Keith Kaap, *In the Eye of the Sphinx: A Perspective on Ethics Research*, 57 Wis. Bar Bull. 14 (June 1984).

other hand, if reasonable, cogent arguments exist on both sides of the proposition, the following factors become significant.

2. *Informed consent*—whether, without compromising the spouses' respective interests, an informed consent by the spouses could resolve the ethical problem. If the spouses' informed consent will resolve the matter, joint representation may be acceptable.
3. *Monetary significance*—the matter's relative significance in monetary terms. This factor considers the relationship between the monetary amount involved and the total present and prospective wealth of one or both spouses. If the amount involved is small in comparison to the spouses' total present and prospective wealth, joint representation may be more acceptable. By contrast, if the amount involved is large in comparison to the total present and prospective wealth, independent representation may be advisable.
4. *Nonmonetary significance*—the matter's significance in terms of its importance in the spouses' relationship, as perceived by the spouses. As under factor 3, if the matter is of minor significance, it may be appropriate for one attorney to represent both spouses; by contrast, if the spouses attach high significance to the matter, the lawyer should exercise more caution, and independent representation may be advisable.
5. *Cost of independent representation*—the increased costs of independent representation (over joint representation), in comparison to the monetary or other significance of the matter. As the monetary or other significance of the matter increases, the weight given to this factor should be reduced. However, if the costs of separate representation are large in comparison to the monetary or other significance of the matter, joint representation is more justifiable. It should be recognized, however, that if conflicts later develop and continuation of joint representation is not possible or advisable, independent representation from the beginning might have been less costly.
6. *Complicating circumstances*—whether complicating circumstances exist, such as children by a prior marriage, disparity in spousal wealth or education, dependent relationship between the spouses, or one or both spouses' lack of knowledge or experience in business, financial, or other matters relevant to the matter involved. Such complicating circumstances suggest that independent representation is advisable.

Conversely, if, for example, the situation involves a first marriage or the absence of children by a prior marriage, little or no disparity in spousal wealth or education, the independence of each spouse in his or her relationship with the other, equal spousal knowledge and experience regarding the matter, or simple and easily understood issues, joint representation may be acceptable.

7. *Irrevocability*—whether the matter involves an irrevocable action or decision or one that can be revoked or changed only by joint spousal action, or whether it involves an action or decision that can be revoked or changed unilaterally by one spouse. If the matter involves an irrevocable decision or one that can be changed only by joint action, that favors independent representation. On the other hand, if the matter involves a decision or action that can be changed or revoked by either spouse acting alone, that favors joint representation.
8. *Prior representation*—the extent of prior representation of one or both spouses by the attorney or his or her law firm. If the attorney previously represented one spouse, independent representation may be preferable. However, if the prior contact was with the spouses jointly, especially if it was longstanding, continuing joint representation may be appropriate.
9. *Judgment of overall fairness*—whether the contemplated action appears to be fair to each spouse rather than one-sided, based on the attorney's good faith, independent judgment. If the contemplated action would have a relatively neutral effect on the parties' interests, joint representation may be acceptable. By contrast, if the contemplated action seems to involve unfairness or overreaching, the attorney should insist on independent representation.

Some commentators have suggested that a lawyer asked to undertake multiple representation of clients should consider interviewing the prospective clients separately to better determine whether the interests of the prospective clients conflict to such a degree that joint representation is inappropriate. See, e.g., John R. Price, *Price on Contemporary Estate Planning* § 1.14, (Supp. 1999) at 11; Hazard, *supra* note 13, at 23.

Further, consistent with SCR 20:2.2, the attorney should strive to accommodate differing interests, promote harmony, and avoid unnecessary discord. This is particularly true in the context of serving spouses. When

appropriate and consistent with the ethical considerations outlined in this chapter, joint representation of spouses should further these ends.<sup>15</sup>

Although the above list includes most of the significant factors involved in reaching a decision on the ethical problems in serving the interests of spouses, other factors may be relevant in a specific case. Moreover, no list can dictate the respective weight to be given to the factors. As with all considerations in resolving ethical questions, the lawyer must apply his or her judgment to the facts of the particular situation.

The factors to consider in determining whether there is a conflict of interest in the estate planning context were addressed in *In the Matter Estate of Koch*, 849 P.2d 977 (Kan. Ct. App. 1993). In *Koch*, two of the testatrix's sons who were disinherited by the operation of an anti-litigation clause in the testatrix's will contested the will's validity. The will provided for an equal distribution of the residue among the testatrix's four sons but also provided that the share of any son in litigation at the time of the testatrix's death as a plaintiff against the testatrix or any of her other sons would be cancelled unless the litigation was dismissed within six weeks following her death. At the time the will was prepared, the two sons who later contested the will were involved as contestants in litigation against the testatrix and her other two sons, who were represented in the litigation by the lawyer who drew up the will. Following the testatrix's death, the contestants refused to dismiss the litigation and sought to have the will set aside on the basis of undue influence.

In attempting to prove undue influence, the contestant sons asserted that the lawyer who drew the will had a conflict of interest because he also represented the other sons in the intrafamily litigation. They argued that the conflict materially limited the lawyer's ability to represent the testatrix and created suspicious circumstances that, when combined with the fiduciary relationship between the lawyer and the testatrix, created a presumption of undue influence. *Id.* at 992.

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<sup>15</sup> See John B. Haydon, *Can One Lawyer Ethically Represent Both Spouses in Estate Planning Under Wisconsin's Marital Property Act?*, Wis. J. Family Law, Sept. 1985, at 12. But see James J. Podell, *The Impact of Wisconsin's Marital Property Act on Marital Agreements: A Divorce Lawyer's Perspective*, Wis. J. Family Law, Sept. 1985, at 10; David L. Walther, *Separate Representation in the Preparation of Marital Agreements*, Wis. J. Family Law, Sept. 1985, at 8. See generally State Bar of Wis., *Lawyers' Marital Property Forum*, Aug. 1985 (newsletter that contains Haydon, Podell, and Walther articles).

In rejecting the contestants' argument that the attorney had a conflict of interest, the court identified and discussed the relevant factors under Kansas Court Rule Annotated 261, which, like Wisconsin SCR 20:1.7, is based on ABA model rule 1.7. The factors identified by the court included the duration and intimacy of the lawyer's relationship with the client(s) involved; the function being performed by the lawyer; the likelihood that an actual conflict will arise; and the likely prejudice to clients if it does arise. *Id.* at 996–97. The court also noted the long-term consideration by the testatrix of her family situation and the fact that her testamentary plan made sense. *Id.* at 998.

In reaching its conclusion that there was no conflict of interest, the court stated:

If we choose to adopt a highly theoretical analysis, it is possible to make an elusive argument and “find” a conflict. If, however, we take a down-to-earth, real world, functional approach in which we insure that confidentiality is preserved and that the client's wishes are served, we are hard pressed to find any ethical violation. . . .

*Id.* at 995. The court further observed:

The scrivener's representation of clients who may become beneficiaries of a will does not by itself result in a conflict of interest in the preparation of the will. Legal services must be available to the public in an economical, practical way, and looking for conflicts where none exist is not of benefit to the public or the bar.

*Id.* at 998.

The case suggests that the factors listed in this section may in some situations be more significant than an overly analytical reading of the text of the Rules of Professional Conduct for Attorneys. *Cf.* section 14.10, *infra*.

### **III. [§ 14.6] Ethical Principles Applicable in the Marital Property Context**

#### **A. [§ 14.7] Identification of Relevant Sections of Rules of Professional Conduct for Attorneys and Related Authority**

Our analysis involves primarily SCR 20:1.7 (Conflict of Interest: general rule), SCR 20:1.9 (Conflict of Interest: former client), and 20:1.6 (Confidentiality of Information). (The nonsequential discussion of these rules in this chapter is intentional, because SCR 20:1.7 involving conflicts of interest, is primary in this consideration.) The ABA model rules, upon which the Rules of Professional Conduct for Attorneys are based, were promulgated with comments adopted with some modifications by the Wisconsin Supreme Court.<sup>16</sup>

Further interpretive assistance may be had in ethics rules of the other community property states,<sup>17</sup> and the prior Wisconsin rules based on the older American Bar Association Model Code of Professional Responsibility.<sup>18</sup>

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<sup>16</sup> The Wisconsin Supreme Court Order adopting the Rules of Professional Conduct for Attorneys states that the comments to the ABA model rules [hereinafter ABA comments] and the comments of Wisconsin's Code of Professional Responsibility Review Committee [hereinafter committee comments] are not adopted but are printed for information purposes. *See* Wis. Sup. Ct. Order, June 10, 1987, 139 Wis. 2d xiii, xv (1987).

<sup>17</sup> The ethics rules in effect in eight of the nine community property states, including Wisconsin, are now based primarily on the ABA model rules. *See ABA/BNA Lawyer's Manual on Professional Conduct* § 01:3 (1983, as supplemented) [hereinafter ABA/BNA Manual]. California is the exception. California attorneys are governed by the California Rules of Professional Conduct, which, although similar to the ABA code, do not contain specifically comparable provisions. *People v. Ballard*, 164 Cal. Rptr. 81 (Ct. App. 1980). In general, the California rules appear to be more practical and specific than the ABA code or ABA model rules, but do not appear to contain provisions uniquely applicable to community property or provisions contrary to the considerations outlined in this chapter. The variations among the ethics rules in the community property states are so extensive that more detailed observations are beyond the scope of this chapter.

<sup>18</sup> Model Code of Professional Responsibility (1984) [hereinafter ABA code]. References to the ABA code's ethical considerations will be indicated as EC-*x*, its disciplinary rules, DR-*x*, and its canons, canon *x* (current rules). References to the

The American Bar Association Commission on the Evaluation of the Rules of Professional Conduct (commonly referred to as the Ethics 2000 Commission) was established in 1997 to comprehensively review and evaluate the ABA Model Rules of Professional Conduct. The changes adopted were influenced by the American Law Institute's *Restatement (Third) of the Law Governing Lawyers*, published in 2000. The Commission recommended significant changes to a number of key rules, such as Rule 1.4 (Communication), Rule 1.6 (Confidentiality of Information), Rule 1.7 (Conflict of Interest: general rule), and Rule 1.8 (Conflict of Interest: prohibited transactions), as well as the adoption of some new rules. The ABA House of Delegates adopted a substantial portion of the Ethics 2000 Commission's recommendations as official ABA policy in February 2002. In addition, the ABA House of Delegates adopted significant changes to Rule 1.6 (Confidentiality of Information).

The Wisconsin Supreme Court Ethics 2000 Committee is currently considering the ABA model rule changes. As of the date of publication the committee appears to be prepared to issue a report adopting the ABA changes almost verbatim. The Wisconsin Supreme Court will consider the committee's report before the changes become effective in Wisconsin, if at all. The details of the ABA changes are discussed in the following sections.

## **B. [§ 14.8] Conflict of Interest**

### **1. [§ 14.9] Various Sources of Guidance**

Wisconsin Supreme Court Rule 20:1.7 is the starting point of any analysis of conflicts of interest. It provides as follows:

SCR 20:1.7 Conflict of interest: general rule

(a) A lawyer shall not represent a client if the representation of that client will be directly adverse to another client, unless:

(1) the lawyer reasonably believes the representation will not adversely affect the relationship with the other client; and

(2) each client consents in writing after consultation.

(b) A lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interests, unless:

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ABA code as previously adopted by Wisconsin will be indicated as former SCR 20.x (rules repealed and replaced effective Jan. 1, 1988).

(1) the lawyer reasonably believes the representation will not be adversely affected; and

(2) the client consents in writing after consultation. When representation of multiple clients in a single matter is undertaken, the consultation shall include explanation of the implications of the common representation and the advantages and risks involved.

SCR 20:1.7 provides the general rule that a lawyer may not represent (absent consent, if appropriate) a client if that representation (1) will be directly adverse to another client's interests, or (2) may be materially limited by the lawyer's responsibility to another client or a third party, or by the lawyer's own interests.<sup>19</sup> In representing two clients at the same time (joint representation—see section 14.4, *supra*) it will be common for one of the above ethics rules to apply.

A lawyer may nonetheless proceed if two conditions are met: (1) the lawyer reasonably believes that the joint representation will not adversely affect either client, and (2) each client consents to the joint representation in writing after consultation.<sup>20</sup> Note that the Wisconsin rule, SCR 20:1.7, requires *written* consent of each client after consultation. It does not require the consultation be in writing, although that may be advisable.

The premise of SCR 20:1.7 is that each client is entitled to the undivided, undiluted loyalty of his or her attorney, as well as to professional

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<sup>19</sup> The following discussion from the *Annotated Code of Professional Responsibility*, despite Wisconsin's adoption of the model rules, remains helpful:

Former canon 6 set forth a concrete definition of "conflicting interests": a conflict was deemed to exist in a situation in which the lawyer had a duty to one client to contend for what his duty to another client required him to oppose. [Then current] DR 5-105 does not contain a comparably clear definition of a proscribed conflict . . . It gives, instead, a two-part test: (1) Is the attorney's independent professional judgment on behalf of a client impaired? or (2) Is the attorney representing "*differing interests*," defined as any interest (conflicting, inconsistent, diverse, or other) which adversely affects either the judgment or the loyalty of the lawyer.

American Bar Found., *Annotated Code of Professional Responsibility* 230–31 (1979) [hereinafter *Annotated Code*] (emphasis in original).

<sup>20</sup> For a discussion of what the consultation must include, see section 14.11, *infra*.



judgment solely for the client's benefit, free of compromising influences and loyalties. *See* SCR 20:1.7 ABA cmt.

In addition, under some circumstances Wisconsin Supreme Court Rule 20:2.2 (Intermediary) may apply.

SCR 20:2.2 Intermediary

(a) A lawyer may act as intermediary between clients if:

(1) the lawyer consults with each client concerning the implications of the common representation, including the advantages and risks involved and the effect on the attorney-client privileges and obtains each client's consent in writing to the common representation;

(2) the lawyer reasonably believes that the matter can be resolved on terms compatible with the clients' best interests, that each client will be able to make adequately informed decisions in the matter and that there is little risk of material prejudice to the interests of any of the clients if the contemplated resolution is unsuccessful; and

(3) the lawyer reasonably believes that the common representation can be undertaken impartially and without improper effect on other responsibilities the lawyer has to any of the clients.

(b) While acting as intermediary, the lawyer shall consult with each client concerning the decisions to be made and the considerations relevant in making them, so that each client can make adequately informed decisions.

(c) A lawyer shall withdraw as intermediary if any of the clients so requests, or if any of the conditions stated in paragraph (a) is no longer satisfied. Upon withdrawal, the lawyer shall not continue to represent any of the clients in the matter that was the subject of the intermediation.

The State Bar of Wisconsin Standing Committee on Professional Ethics provided a useful analysis of the interaction of SCR 20:1.7 and SCR 20:2.2 when it addressed in an opinion the issue of independent representation of both the majority and minority investors in connection with the formation of a business.<sup>21</sup>

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<sup>21</sup> In State Bar of Wisconsin Standing Committee on Professional Ethics, Formal Opinion E-89-10 (1989) (Conflicts: Representing Majority and Minority Investors in New Business Formation), the committee determined that, generally, one lawyer (or law firm) may represent both the majority and minority investors in connection with the formation of a business (for example, a partnership or corporation), if the standards and procedures of SCR 20:1.7 (conflict of interest) and SCR 20:2.2 (intermediary) are satisfied. The committee recognized the propriety of such dual representation under appropriate circumstances, but strict compliance with both SCR 20:2.2 (including consideration of the relevant factors in determining whether the dual representation is appropriate) and SCR 20:1.7(b)

In addition, Wisconsin Supreme Court Rule 20:1.9 defines conflicts of interest with respect to former clients. *See infra*, section 14.12.

These rules also apply to the lawyer's partners or the associates of his or her firm, so that if the lawyer may not serve under SCR 20:1.7 or SCR 20:1.9, neither may the lawyer's partners or his or her associates or firm. *See* SCR 20:1.10.

Because the rules were developed primarily for a litigation or other adversarial context, rather than for a family, spousal, or similar context, it is often very difficult to apply these rules to specific situations involving representation of one or both spouses (or other family members) in a non-litigation context (in which the rule may be more easily understood and its application may be clear).

The ABA comments and the comments of the Code of Professional Responsibility Review Committee following each rule provide some guidance, although these comments were not formally adopted by the Wisconsin Supreme Court.<sup>22</sup> The comments following SCR 20:1.7 suggest that the critical questions involve the likelihood that a conflict of interest will occur, and if it does, whether it will materially interfere with the lawyer's independent professional judgment. Unfortunately, with respect to estate planning and probate the comments simply provide as follows:

A lawyer may be called upon to prepare wills for several family members, such as husband and wife, and, depending upon the circumstances, a conflict of interest may arise. In estate administration the identity of the client may be unclear under the law of a particular jurisdiction. Under one view, the client is the fiduciary; under another view the client is the estate or trust, including its beneficiaries. The lawyer should make clear the relationship to the parties involved.

SCR 20:17 comment.

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(obtaining the clients' informed consent) is required. The committee also concluded that written consent to the representation is required under SCR 20:1.7(b) after appropriate explanation. *See infra* § 14.11. The committee further concluded that, if withdrawal from dual representation is required, SCR 20:2.2(c) requires that the lawyer not continue to represent either client. The committee stated that SCR 20:2.2(c) is an exception to the general rule of SCR 20:1.9(a), which permits dual representation if the former client consents.

<sup>22</sup> *See* Wis. Sup. Ct. Order, June 10, 1987, 139 Wis. 2d xiii, xv (1987).

To provide assistance to trusts and estates lawyers, courts, and other persons in interpreting the ABA model rules, including rule 1.7 on conflicts of interest, the American College of Trust and Estate Counsel has adopted the *ACTEC Commentaries*, discussed at section 14.4, *supra*. Though the Commentaries do not constitute an official interpretation of the model rules, they seek to identify ways in which common ethical issues under the rules might be dealt with by trusts and estates lawyers.

In addition, the Special Study Committee on Professional Responsibility of the ABA Section of Real Property, Probate and Trust Law has offered views on various professional responsibility issues that may arise in the simultaneous representation of spouses, in its report *Representing Husband and Wife*, discussed at section 14.4, *supra*. The report takes the position that joint representation of husband and wife does not necessarily implicate rule 1.7. Rather, the report concludes that rule 1.7 applies only once the lawyer discerns that there is a substantial potential for a material limitation upon the lawyer's representation of either spouse. *Representing Husband and Wife*, *supra* note 5, at 779–80. Like the *ACTEC Commentaries*, the special committee report does not constitute official commentary on the model rules, and it has been criticized for some of its views.

An excellent source for guidance in ethical matters is the *ABA/BNA Lawyer's Manual on Professional Conduct*. Under the heading "Practice Guide, Multiple Representation," the following general statements are made:

[T]he rules and law are clear that a lawyer may [represent multiple parties in the same transaction] only under very limited circumstances, namely, where the lawyer reasonably believes the multiple representation will not adversely affect any one of the clients, and all of the clients consent after full disclosure of the implications of the multiple representation.

These limitations thus make it very unlikely, and perhaps impossible, for a lawyer to ever represent opposing parties in litigation or multiple parties to the same transaction whose interests or positions are fundamentally antagonistic. But they do make it permissible for a lawyer to represent multiple parties whose interests are generally aligned, such as clients with similar lobbying interests or parties to the formation of a corporation. However, should it become evident during the multiple representation that the lawyer cannot adequately represent the interests of each party, or should any party revoke consent, the lawyer must then withdraw and may not thereafter represent one party against another on the same matter.

ABA/BNA Manual, *supra* note 17, at 51:301.

Another source of general guidance is the American Law Institute's *Restatement (Third) of the Law Governing Lawyers*.<sup>23</sup> Section 121, entitled "Conflicts of Interest—In General" roughly corresponds with SCR 20:1.7(b), dealing with conflicts other than those involving concurrent representation of adverse clients. Section 130, entitled "Multiple Representation in Non-Litigated Matter," roughly corresponds with SCR 20:1.7(a), dealing with conflicts between directly adverse clients and with SCR 20:2.2, dealing with intermediary representations. The Restatement may be particularly useful in analyzing conflicts under the newly revised ABA model rules, which may well become applicable to Wisconsin lawyers in the very near future. The ABA's revised rules were developed in close coordination with the Restatement.

The ABA's recently adopted changes to the Model Rule of Professional Responsibility include a substantially revised rule 1.7. The Wisconsin Supreme Court Ethics 2000 Committee is likely to favorably report on the new rule.

**Rule 1.7: Conflict Of Interest: Current clients**

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

- (1) the representation of one client will be directly adverse to another client; or
- (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

- (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
- (2) the representation is not prohibited by law;
- (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and
- (4) each affected client gives informed consent, confirmed in writing.

Note that the revised rule provides that a lawyer shall not represent a client if the representation of that client may be "materially limited" by the

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<sup>23</sup> ALI, *Restatement (Third) of the Law Governing Lawyers* (2000) [hereinafter Restatement].

lawyer's other responsibilities only if there is a "substantial risk" of such material limitation. Rule 2.2 (Intermediary) is eliminated in the new rules and the requirements of that rule are largely subsumed in the concept of "concurrent conflict of interest" found in the revised rule 1.7.

## **2. [§ 14.10] Suggested Analytical Framework for Conflicts of Interest**

It may be helpful to attempt to parse the requirements of SCR sections 20:1.7 and 20:2.2. The first step is to analyze whether a conflict exists at all. If it does, the next step is to determine what standards apply in addressing the conflict.

1. *No Conflict.* Some authority exists to suggest that under certain circumstances, a joint representation of spouses presents no conflict of interest. The importance of such a determination is that it obviates, in such cases the need to obtain the client's written consent after consultation or to comply with the other requirements of SCR sections 20:1.7 and 20:2.2. However, the lawyer must continue to monitor whether the determination that no conflict of interest is present remains supportable throughout the representation.

The illustrations under Restatement section 130, entitled "Multiple Representation in Non-Litigated Matter," specifically contemplate joint representation of spouses in estate planning and take the position that, in some situations, the joint representation does not involve a conflict and therefore does not require client consent. The illustrations go on to suggest, however, that other such situations may present a conflict and therefore require informed consent to proceed with joint representation of the spouses.<sup>24</sup>

Montana Ethics Opinion 960731 (1996) takes the position that, absent an existing conflict or evidence that the lawyer's independent judgment will likely be adversely influenced by jointly representing spouses with their estate planning, the lawyer need not communicate to the couple the potential for conflicts of interest under rule 1.7 of the model rules, nor obtain a written conflict waiver. Nonetheless, the opinion goes on to

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<sup>24</sup> Restatement, § 130, Illustrations 1 and 2.

observe, “we believe that for the lawyer’s purpose it is wise practice to obtain a written waiver.”<sup>25</sup>

In Florida Ethics Opinion 95-4 the Board of Governors of the Florida bar concluded that, when jointly representing a husband and wife in estate planning (see *infra* section 14.13 for a more detailed fact pattern), the lawyer was not ethically required to discuss the lawyer’s obligations with regard to separate confidences with the husband and wife. The Board observed that while such a discussion is not ethically required, in some situations it might help prevent the type of occurrence that was the subject of the opinion.

Even if an attorney concludes that SCR 20:1.7 does not apply to a particular joint representation and chooses not to make the disclosures and obtain the consents required thereunder, the lawyer should monitor the client relationship to determine whether circumstances develop that implicate the rule.

2. *Representation Materially Limited.* Many joint representations will fall within the ambit of SCR 20:1.7(b). In many joint representations the representation of one of the spouses may be materially limited by the lawyer’s responsibilities to the other spouse when counseling them with respect to their respective rights in marital property.

There are two variations of this conflict situation. One is when the lawyer proposes to represent both spouses (for example in estate planning) and also represents or proposes to represent one of the spouses in a separate matter, which representation will be materially limited by the lawyer’s responsibilities to the other spouse. In such a case, SCR 20:1.7(b) would apply, but not SCR 20:2.2, because the latter rule only applies to representations of clients in the same matter. If, however, the lawyer represents both spouses in a matter and the representation will be materially limited by the lawyer’s responsibilities in that matter to either spouse, then both SCR 20:1.7(b) and SCR 20:2.2 should apply.

The comments to the revised ABA model rule 1.7 provide some insight:

Even where there is no direct adverseness, a conflict of interest exists if there is a significant risk that a lawyer’s ability to consider, recommend or carry out

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<sup>25</sup> The opinion can be viewed online at <http://www.montanabar.org> (follow the links to the 1996 ethics opinions). As of the date of publication the direct link is <http://www.montanabar.org/ethics/ethics/ethicsopinions/960731.html>

an appropriate course of action for the client will be materially limited as a result of the lawyer's other responsibilities or interests. For example, a lawyer asked to represent several individuals seeking to form a joint venture is likely to be materially limited in the lawyer's ability to recommend or advocate all possible positions that each might take because of the lawyer's duty of loyalty to the others. The conflict in effect forecloses alternatives that would otherwise be available to the client. The mere possibility of subsequent harm does not itself require disclosure and consent. The critical questions are the likelihood that a difference in interests will eventuate and, if it does, whether it will materially interfere with the lawyer's independent professional judgment in considering alternatives or foreclose courses of action that reasonably should be pursued on behalf of the client.

ABA Model Rule section 1.7 cmt. 8.

One of the ways a representation may be materially limited is by the lawyer's own interests. A number of specific lawyer-interest situations are covered by SCR 20:1.8 (Conflict of Interest: prohibited transactions). SCR 20:1.8 provides specific consent requirements for some of these instances. For example, it must be recognized that the person who pays the fees has the power to exert pressure that affects the lawyer's independent judgment. *See* SCR 20:1.8(f), :5.4(c). The rules prohibit a lawyer from accepting compensation for representation from a person other than a client unless there is no interference with the lawyer's independent professional judgment or the lawyer-client relationship, the client consents after consultation, and information relating to the representation is protected as required by SCR 20:1.6. SCR 20:1.8(f).

3. *Representation Directly Adverse.* Under some circumstances the interests of the jointly represented spouses may be directly adverse. There are two variations of this conflict situation. One is when the lawyer proposes to represent both spouses (for example in estate planning) and also represents or proposes to represent one of the spouses in a separate matter in which the other spouse has a directly adverse interest. In such a case, SCR 20:1.7(a) is implicated, but not SCR 20:2.2, because the latter rule only applies to representations of clients in the same matter. In cases in which the lawyer represents both spouses in the matter in which their interests are directly adverse, then both SCR 20:1.7(a) and SCR 20:2.2 are implicated.

The comments to the revised ABA model rule 1.7 provide some insight:

[A]bsent consent, a lawyer may not act as an advocate in one matter against a person the lawyer represents in some other matter, even when the matters are

wholly unrelated. The client as to whom the representation is directly adverse is likely to feel betrayed, and the resulting damage to the client-lawyer relationship is likely to impair the lawyer's ability to represent the client effectively. In addition, the client on whose behalf the adverse representation is undertaken reasonably may fear that the lawyer will pursue that client's case less effectively out of deference to the other client, i.e., that the representation may be materially limited by the lawyer's interest in retaining the current client.

ABA Model Rule section 1.7 cmt. 6.

4. *Intermediation.* If the jointly represented spouses are directly adverse (or the representation of one of the spouses may be materially limited by the lawyer's responsibilities to the other spouse) *and* the lawyer is representing them *both* in the matter, then the requirements of SCR 20:2.2 must also be met.

The ACTEC Commentary on Model Rule 2.2 briefly addresses the applicability of the intermediary rule in an estate planning context:

If it appears appropriate to the lawyer, the lawyer may act as an intermediary between clients with respect to trusts and estates matters. For example, intermediation may be appropriate with respect to estate or trust administration matters, or representation in connection with a family business enterprise, which may involve clients with actual or potentially conflicting interests, but more important common goals... Note, however, that most common representations do not involve intermediation under MRPC 2.2. The representation of multiple clients in estate planning and administration matters including the representation of multiple fiduciaries is not ordinarily provided pursuant to MRPC 2.2.

Note that under the revised ABA model rules, rule 2.2 has been eliminated and the issues it deals with are incorporated in model rule 1.7 (dealing with joint representation) and new model rule 2.4 (dealing with the lawyer as a mediator). This rule change is currently under consideration in Wisconsin and may affect Wisconsin lawyers in the near future. See the discussion at section 14.9, *supra*.

5. *Reasonable Belief and Consent.* If a conflict exists, either because the spouses that are to be jointly represented are directly adverse (SCR 20:1.7(a)) or because the lawyer's representation of one spouse is materially limited by responsibilities to the other spouse, then two requirements are imposed upon the lawyer before the joint representation may proceed.



First, the lawyer must meet a “reasonable belief” requirement. In the case of the directly adverse conflict (SCR 20:1.7(a)) the lawyer must reasonably believe that the representation will not adversely affect the relationship with the “other” client. If the representation of one of the spouses may be materially limited by the lawyer’s responsibilities to the other spouse (SCR 20:1.7(b)), the lawyer must reasonably believe that the representation will not adversely affect the representation of the spouse being represented in the particular matter.

Second, the lawyer must obtain written consent from the affected clients after consultation. *See infra* section 14.11.

6. *Enhanced Requirements for Intermediation.* If the intermediation rules apply, then in addition to complying with the “reasonable belief” and “written consent after consultation” requirements of SCR 20:1.7, the lawyer must meet the enhanced requirements of SCR 20:2.2. The enhanced requirements expand on the “reasonable belief” and “written consent after consultation” requirements of SCR 20:1.7. The enhanced “reasonable belief” requirements are:

[T]he lawyer reasonably believes that the matter can be resolved on terms compatible with the clients’ best interests, that each client will be able to make adequately informed decisions in the matter and that there is little risk of material prejudice to the interests of any of the clients if the contemplated resolution is unsuccessful; and

[T]he lawyer reasonably believes that the common representation can be undertaken impartially and without improper effect on other responsibilities the lawyer has to any of the clients.

SCR 20:2.2(a)(2) and (3). The enhanced consent/consultation requirements are:

[T]he lawyer consults with each client concerning the implications of the common representation, including the advantages and risks involved and the effect on the attorney-client privileges and obtains each client’s consent in writing to the common representation.

While acting as intermediary, the lawyer shall consult with each client concerning the decisions to be made and the considerations relevant in making them, so that each client can make adequately informed decisions.

SCR 20:2.2(a)(1) and (b).

Note again that under the revised ABA model rules, rule 2.2 has been removed and the issues it deals with are incorporated in model rule 1.7 and new model rule 2.4. This rule change may soon be considered by the Wisconsin Supreme Court.

7. *Independent Representation Required.* If SCR 20:1.7 (and possibly SCR 20:2.2) is implicated and (1) the representation does not meet the “reasonable belief” requirements, (2) consultation cannot occur, or (3) written consent is not given, then the lawyer may not accept the joint representation and must insist that the clients obtain independent representation.

The above analytical framework may seem somewhat at odds with the spirit of the factors laid out in section 14.5, *supra* (see *In re Estate of Koch*, *supra* section 14.5). In fact, these approaches are readily synthesized by treating the factors laid out in section 14.5, *supra*, as the basis upon which the lawyer may determine whether the subjective standards set out in SCR 20:1.7 are satisfied; i.e. whether a representation may be “materially limited” and whether the lawyer may “reasonably believe” the clients’ interests will not be adversely affected by going forward with the representation.

### 3. [§ 14.11] Consent to Joint Representation

A proposed joint representation could be beneficial to one spouse and directly adverse to the other’s interests, or the representation could be materially limited by the attorney’s responsibilities to others, including responsibilities to one of the spouses. After considering and applying SCR 20:1.7 and the factors outlined in section 14.5, *supra*, the lawyer may nonetheless be able to represent both spouses (joint representation), if the lawyer reasonably believes that representation of neither spouse will be adversely affected. See *supra* section 14.10.<sup>26</sup>

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<sup>26</sup> The new ABA model rule 1.7 (currently under consideration in Wisconsin—see *supra* section 14.9) changes the terminology from “consent after consultation” to “informed consent.” The ABA definition of informed consent appears to be more stringent than the current Wisconsin standard: “‘Informed consent’ denotes the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct.” ABA model rule 1.0(e). The new comments elaborate that:

In addition, such a joint representation requires each client's consent in writing after consultation. The lawyer must advise each spouse of the conflict or potential conflict and its implications and the advantages and risks of common representation; the lawyer also must give each spouse the chance to evaluate his or her need for independent representation free of potential conflict. The lawyer may proceed to jointly represent the spouses only if each spouse then provides written consent.

An attorney cannot accept the spouses' consent to joint representation until appropriate and adequate consultation has been provided to each spouse, whether by that attorney or another attorney. Consultation concerning joint representation must include an explanation of the implications, advantages, and risks of joint representation. SCR 20:1.7(a)(2), (b)(2).

The ABA comment contains a "test" for whether a consent to a conflict of interest is possible, which can be characterized as the "disinterested lawyer" test:

A client may consent to representation notwithstanding a conflict. However, . . . when a disinterested lawyer would conclude that the client should not agree to the representation under the circumstances, the lawyer involved cannot properly ask for such agreement or provide representation on the basis of the client's consent. . . . Moreover, there may be circumstances where it is impossible to make the disclosure necessary to obtain consent. For example, when the lawyer represents different clients in related matters and one of the clients refuses to consent to the disclosure necessary to permit the other client to make an informed decision, the lawyer cannot properly ask the latter to consent.

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"[i]nformed consent requires that each affected client be aware of the relevant circumstances and of the material and reasonably foreseeable ways that the conflict could have adverse effects on the interests of that client... . The information required depends on the nature of the conflict and the nature of the risks involved. When representation of multiple clients in a single matter is undertaken, the information must include the implications of the common representation, including possible effects on loyalty, confidentiality and the attorney-client privilege and the advantages and risks involved." ABA Model Rule § 1.7 cmt. 18.

SCR 20:1.7 ABA cmt. (Consultation and Consent).<sup>27</sup>

Although the above comment concerning revocation of consent may be correct as a general statement, it is not universally applicable, especially in a nonlitigation context. *See infra* § 14.12.<sup>28</sup>

The ACTEC Commentary on Model Rule 1.7 (Conflict of Interest: General Rule), discussed at section 14.4, *supra*, notes that some conflicts are so serious that the informed consent of the parties is insufficient. When the interests of clients actually conflict to such a degree that the lawyer cannot adequately represent their individual interests, the lawyer should not undertake joint representation. The Commentary cites as one example of such a situation the representation of both parties to a prenuptial agreement. Presumably the example refers to a prenuptial agreement that addresses divorce or otherwise involves the significant waiver of spousal rights. *ACTEC Commentaries*, *supra* note 10.

Section 130 of the Restatement recognizes that a lawyer may represent multiple clients notwithstanding an otherwise prohibited conflict if the

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<sup>27</sup> The comments to the recently revised ABA model rules address whether a conflict can be consented to:

Consentability is typically determined by considering whether the interests of the clients will be adequately protected if the clients are permitted to give their informed consent to representation burdened by a conflict of interest. Thus... representation is prohibited if in the circumstances the lawyer cannot reasonably conclude that the lawyer will be able to provide competent and diligent representation.

ABA Model Rule § 1.7 cmt. 15.

<sup>28</sup> The new comments to the revised ABA model rules add the following guidance:

A client who has given consent to a conflict may revoke the consent and, like any other client, may terminate the lawyer's representation at any time. Whether revoking consent to the client's own representation precludes the lawyer from continuing to represent other clients depends on the circumstances, including the nature of the conflict, whether the client revoked consent because of a material change in circumstances, the reasonable expectations of the other client and whether material detriment to the other clients or the lawyer would result.

ABA Model Rule § 1.7 cmt. 21.

affected clients give informed consent in accordance with the requirements of section 122 of the Restatement. The illustrations under section 130, however, make quite clear the view that the simultaneous representation of a husband and wife in estate planning does not per se present a conflict of interest situation. *See supra* § 14.10.<sup>29</sup>

#### **4. [§ 14.12] Representing One Spouse Following Joint Representation**

A related issue is whether, when independent representation is required, an attorney who previously represented the spouses jointly may represent one of them in the same or a related matter. The test seems to be whether, in accepting the subsequent representation, the attorney, in furthering the interests of the new client, may be required to do anything that will injure the former client in any matter in which he or she formerly represented the client, or whether the attorney may be called upon to use any knowledge or information acquired in the course of that representation against the former client. Drinker, *supra* note 7, at 105.

The ABA comments to model rule 1.9 (SCR 20:1.9) indicate that information acquired by a lawyer in the course of representing a client generally may not subsequently be used by the lawyer to the client's

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<sup>29</sup> The new comments to the revised ABA model rules provide:

“[A] lawyer may not represent multiple parties to a negotiation whose interests are fundamentally antagonistic to each other, but common representation is permissible where the clients are generally aligned in interest even though there is some difference in interest among them. Thus, a lawyer may seek to establish or adjust a relationship between clients on an amicable and mutually advantageous basis; for example, in helping to organize a business in which two or more clients are entrepreneurs, working out the financial reorganization of an enterprise in which two or more clients have an interest or arranging a property distribution in settlement of an estate. The lawyer seeks to resolve potentially adverse interests by developing the parties' mutual interests. Otherwise, each party might have to obtain separate representation, with the possibility of incurring additional cost, complication or even litigation. Given these and other relevant factors, the clients may prefer that the lawyer act for all of them.”

ABA Model Rule § 1.7 cmt. 28.

disadvantage. However, the fact that the lawyer once served the client does not preclude the lawyer from using “generally known” information about the client when later representing another client. SCR 20:1.9, ABA cmt. Further, disqualification from subsequent representation can be waived, but only if the circumstances of the intended representation are disclosed. *Id.*

In general, in an adversarial context or when a dispute arises concerning the subject matter of prior representation, the attorney who previously represented the spouses jointly may not represent one of them unless the spouse who is no longer represented by the attorney consents. The guidelines for consent in this situation are the same ones used in consenting to joint representation. *See supra* § 14.11. The consent should be in writing, and if there is also independent counsel, the consent should recite that it is given after consultation with that spouse’s independent counsel.<sup>30</sup>

In State Bar of Wisconsin Standing Committee on Professional Ethics, Formal Opinion E-89-4 (1989) (Prior Joint Representation of Spouses and Subsequent Representation of One Spouse in Divorce Action), the committee concluded that under SCR 20:1.9(a), unless the former client spouse consents to representation adverse to him or her after consultation,

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<sup>30</sup> The new comments to the revised ABA model rules provide as follows:

“Whether a lawyer may properly request a client to waive conflicts that might arise in the future is subject to the test of [section 1.7(b)]. The effectiveness of such waivers is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails. The more comprehensive the explanation of the types of future representations that might arise and the actual and reasonably foreseeable adverse consequences of those representations, the greater the likelihood that the client will have the requisite understanding. Thus, if the client agrees to consent to a particular type of conflict with which the client is already familiar, then the consent ordinarily will be effective with regard to that type of conflict. If the consent is general and open-ended, then the consent ordinarily will be ineffective, because it is not reasonably likely that the client will have understood the material risks involved. On the other hand, if the client is an experienced user of the legal services involved and is reasonably informed regarding the risk that a conflict may arise, such consent is more likely to be effective, particularly if, e.g., the client is independently represented by other counsel in giving consent and the consent is limited to future conflicts unrelated to the subject of the representation. In any case, advance consent cannot be effective if the circumstances that materialize in the future are such as would make the conflict nonconsentable under [section 1.7(b)].”

ABA Model Rule § 1.7 cmt. 22.

the law firm that had previously represented both spouses in general legal matters (including assistance in purchasing assets subject to property division) could not represent one of the spouses in a subsequent divorce action. This conclusion was drawn because the prior representation was connected with matters substantially related to the divorce, in which one spouse's interest would be materially adverse to the other spouse's interest. The committee stated that a substantial relationship between the matters exists "if the factual contexts of the two representations are similar or related." *Id.*

The Restatement takes a similar approach:

**§ 132. Representation Adverse to Interest of Former Client**

Unless both the affected present and former clients consent to the representation under the limitations and conditions provided in § 122, a lawyer who has represented a client in a matter may not thereafter represent another client in the same or a substantially related matter in which the interests of the former client are materially adverse. The current matter is substantially related to the earlier matter if:

- (1) the current matter involves the work the lawyer performed for the former client; or
- (2) there is a substantial risk that representation of the present client will involve the use of information acquired in the course of representing the former client, unless that information has become generally known.

Restatement, *supra* note 23, at § 132.

In Delaware Board Case No. 102 (1998), the Preliminary Review Committee of the Board of Professional Responsibility privately admonished a lawyer for preparing a new will for a wife that excluded her husband as a beneficiary after the lawyer had jointly represented the husband and wife in several legal matters. The wife requested the change in her will after the husband filed for divorce.

### **C. [§ 14.13] Client Confidences**

Wisconsin Supreme Court Rule 20:1.6(a) provides that "[a] lawyer shall not reveal information relating to representation of a client unless the client consents after consultation, except for disclosures that are impliedly authorized in order to carry out the representation . . . ." The policy behind this rule is that a client needs to be free to discuss any matter with his or her lawyer, and that a lawyer should be equally free to obtain information from the client. SCR 20:1.6 ABA cmt. Confidences must be preserved

even after termination of the attorney-client relationship. SCR 20:1.6 ABA cmt. (Former Client). However, a lawyer may reveal information when necessary to perform the attorney's services, when required by law, or when the client consents after full disclosure. SCR 20:1.6(a). In addition, a lawyer shall disclose information to prevent or rectify a client's criminal or fraudulent acts that the lawyer reasonably believes are likely to result in death or substantial bodily harm or substantial injury to the financial interest or property of another. SCR 20:1.6(c).

Particularly relevant to relationships between spouses is the rule that a lawyer may not use information gained in the course of representation to the client's disadvantage. SCR 20:1.8(b), .9(b). For example, an attorney who represented one of the spouses before or during their marriage later may be asked to represent them both in connection with the subject matter of the first representation. The attorney should alert the first spouse to this rule and its implications and give the first spouse the opportunity to grant or deny consent to the joint representation. Conversely, the same considerations apply when the attorney may have represented both spouses during their marriage and then is asked to represent one of them in connection with the same subject matter. *See supra* § 14.12.

These rules apply not only to information protected by the attorney-client privilege but also to information gained in the professional relationship that the client has requested be kept confidential, as well as to any information that if disclosed is likely to be embarrassing or detrimental to the client. Indeed, the expansive language of SCR 20:1.6 implies that the information protected in the attorney-client relationship is *any* information relating to the representation.

The common representation of a husband and wife, either jointly or as separate clients, *see supra* § 14.4, raises the question of the lawyer's disclosure of confidential communications imparted to the lawyer by only one spouse. The majority view is that, absent an agreement to the contrary, common representation of spouses is "joint," and that communications to the lawyer by either spouse, though confidential as to third parties, are not confidential as between the spouses. *See Ross, supra* note 11, at 16–17. The lawyer is thus placed in a difficult situation upon receiving a confidential communication from one spouse that that spouse does not wish to have shared with the other spouse.

The ACTEC Commentary on Model Rule 1.6 (Confidentiality of Information) offers alternatives for the lawyer who receives a confidence



from one common client who opposes its disclosure to another common client. The Commentary asserts that, in such cases, the lawyer should have a reasonable degree of discretion in determining how to respond to any particular case. *See ACTEC Commentaries, supra* note 10.

The ACTEC Commentary on Model Rule 1.6 concurs with the view espoused in the report by the Special Study Committee on Professional Responsibility of the Section of Real Property, Probate and Trust Law that it is advisable to obtain in advance an agreement with husband and wife (preferably in writing) regarding the “ground rules” of the representation.<sup>31</sup>

The Supreme Court of New Jersey faced the issue of disclosure of confidential information between spouses in a joint representation in *A. v. B.*, 726 A.2d 924 (N.J. 1999). After preparing a coordinated estate plan for a husband and wife, a law firm inadvertently took on the representation of a different woman who had filed a paternity suit against the husband. When the firm discovered the conflict, it notified the husband of its intention to tell his wife, the firm’s joint client, about the paternity suit. At that point the husband sought to enjoin the firm from disclosing the information, and was successful in the lower court. Ultimately, however, the supreme court ruled that the firm was entitled to disclose the existence (but not the identity) of the husband’s nonmarital child. The court reasoned that the husband had in effect committed a fraud on his wife by failing to disclose the existence of the child in the context of the joint estate planning process, which the firm was entitled to rectify under New Jersey RPC 1.6(c). Like Wisconsin, New Jersey adopted model rule 1.6 with modifications that supported the disclosure to the wife.

Florida Ethics Opinion 95-4 takes a contrary approach to disclosure. The summary of the opinion states:

In a joint representation between husband and wife in estate planning, an attorney . . . may not reveal confidential information to the wife when the husband tells the attorney that he wishes to provide for a beneficiary that is unknown to the wife. The attorney must withdraw from the representation of

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<sup>31</sup> *ACTEC Commentaries, supra* note 10. *See generally Representing Husband and Wife, supra* note 5; *see also* Teresa S. Collett, *Disclosure, Discretion, or Deception: The Estate Planner’s Ethical Dilemma From a Unilateral Confidence*, 28 Real Prop. Prob. & Tr. J. 683 (1994); Jeffrey N. Pennell, *Professional Responsibility: Reforms Are Needed to Accommodate Estate Planning and Family Counselling*, 25 *The Annual Phillip E. Heckerling Institute on Estate Planning* § 1805.1 (1991). *See also* the references cited at section 14.5, *supra*.

both husband and wife because of the conflict presented when the attorney must maintain the husband's separate confidences regarding the joint representation.<sup>32</sup>

As suggested in the sample letters appearing in sections 14.35–.36, *infra*, the issue of sharing confidential communications can be addressed at the outset of the attorney-client engagement as part of the written consent to the joint representation arrangement.

For further discussion regarding the permissive disclosure of confidential client information to prevent, rectify or mitigate substantial financial loss, see Restatement *supra* note 23, § 67.

With limited exceptions, the lawyer's duty of confidentiality arising from the common law attorney-client privilege survives the client's death. See *Swidler & Berlin v. United States*, 524 U.S. 399 (1998) (handwritten notes of attorney made nine days before Deputy White House Counsel Vincent W. Foster, Jr. committed suicide were not discoverable by Independent Counsel in Whitewater investigation of Clinton administration).

#### **D. [§ 14.14] Avoidance of Appearance of Professional Impropriety**

The principles of ABA code canon 9 are incorporated into most of the current Rules of Professional Conduct for Attorneys and the preamble, although they are not specifically designated as a separate rule. Canon 9 provides that “[a] lawyer should avoid even the appearance of professional impropriety.” This canon is based on the concept that a lawyer should promote public confidence in the legal system and the profession. Hence, for example, as stated in the preamble to the current Rules of Professional Conduct for Attorneys, a lawyer's conduct should “conform to the requirements of the law, both in professional service to clients and in the lawyer's business and personal affairs.” The preamble also states that it is a lawyer's duty to uphold the legal process: “As a public citizen, a lawyer

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<sup>32</sup> Fla. Eth. Op. 95-4 (May 30, 1997). As of the date of publication the direct link is <http://www.flabar.org/tfb/tfbetopin.nsf/SearchView/Ethics,+OPINION+95-4?opendocument>. For a discussion of the history and import of Advisory Opinion 95-4, see Hollis F. Russell & Peter A. Bicks, *Joint Representation of Spouses in Estate Planning: The Saga of Advisory Opinion 95-4*, Fla. Bar J. (March 1998).

should seek improvement of the law, the administration of justice and the quality of service rendered by the legal profession.” The formulation under the ABA code is that a lawyer should try to reflect credit on the profession and should try to inspire the confidence, respect, and trust of his or her clients. In serving these ends, the code says, the attorney should “strive to avoid not only professional impropriety but also the appearance of impropriety.” Former SCR 20.48(6) (EC 9 6).

Although the Rules of Professional Conduct for Attorneys do not include a specific section incorporating the old “appearance of professional impropriety” canon, the Wisconsin Court of Appeals has held that its standard was retained in the Rules. In *Burkes v. Hales*, 165 Wis. 2d 585, 478 N.W.2d 37 (Ct. App. 1991), the court stated as follows:

In [*Berg v. Marine Trust Co.*, 141 Wis. 2d 878, 416 N.W.2d 643 (Ct. App. 1987)], we recognized that lawyers have the duty “to ‘preserve the confidences and secrets of a client’ and to ‘avoid . . . even the appearance of professional impropriety.’” *Id.*, 141 Wis. 2d at 886, 416 N.W.2d at 647, quoting *Westinghouse Elec. v. Gulf Oil*, 588 F.2d at 224. We noted that such a rule embodies the substance of Canons 4 and 9 of the A.B.A. Code of Professional Responsibility which appeared in our own code as SCR 20.21 and 20.48 (1986). *Id.* Wisconsin adopted the A.B.A.’s Model Rules of Professional Responsibility in 1987. These rules, which replaced those in effect when *Berg* was decided, omit the appearance of impropriety language. According to the comments accompanying the new rules, the language was deleted for two reasons:

First, the appearance of impropriety can be taken to include any new client-lawyer relationship that might make a former client feel anxious. If that meaning were adopted, disqualification would become little more than a question of subjective judgment by the former client. Second, since impropriety is undefined, the term “appearance of impropriety” is question begging.

Nevertheless, at least one other jurisdiction adopting the new rules believes it is still appropriate to consider the “appearance of impropriety” when weighing ethical matters because “its meaning pervades the Rules and embodies their spirit.” *First American Carriers, Inc., v. Kroger Co.*, 787 S.W.2d 669, 672 (Ark. 1990).

We see no error in the trial court’s decision [in holding the lawyer disqualified]. First, there is no indication that the court placed undue or even substantial reliance on appearances of impropriety in arriving at its decision. Second, while we recognize that the mere appearance of impropriety, without more, will no longer disqualify an attorney, we agree with our colleagues on the Arkansas court that the spirit of that standard survives as a useable and useful guide for making ethical decisions. . . . Despite deletion of the “appearance” language from the code of ethical

conduct, we continue to believe that considerations of “the lay sense of justice” are implicit in the new rules. *Berg*, 141 Wis. 2d at 890–91, 416 N.W.2d at 649, citing *Marketti v. Fitzsimmons*, 373 F. Supp. 637, 639 (W.D. Wis. 1974).

*Id.* at 599–600.<sup>33</sup>

In sum, lawyers faced with the decision to serve as counsel for both spouses have the duty to be alert to the ethical ramifications and considerations involved. They also have the responsibility to resolve any ethical problems in a manner consistent with the principles of the Rules of Professional Conduct for Attorneys and the interests of each spouse.

Although the model rules contain no precise counterpart of canon 9, this deletion has not eliminated the concept that a lawyer should avoid even the appearance of impropriety. Indeed, the import of canon 9 is reflected throughout the entire model rules and is alluded to in the preamble. *See* Rules of Professional Conduct for Attorneys.

## **E. [§ 14.15] Aspects of Marital Property Law With Ethical Significance For Joint Representation of Spouses**

### **1. [§ 14.16] Elements of Marital Property**

#### **a. [§ 14.17] In General**

The following elements of Wisconsin marital property create situations in which joint representation raises ethical problems. These situations under marital property also illustrate instances in which lawyers must be alert to ethical concerns. In these situations, the lawyer must consider whether separate representation, joint representation based on informed consent, or other action is ethically required.

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<sup>33</sup> The court of appeals also cited David Ivers, *Prohibition Against Appearance of Impropriety Retained Under Model Rules of Professional Conduct*, 13 U. Ark. Little Rock L.J. 271, 282 (1991). *See* 165 Wis. 2d 598 n.9.

**b. [§ 14.18] Ownership and Classification**

Under common law, because ownership is usually based on title, the spouses generally understand (or easily can determine) who owns specific assets, and a lawyer can give relatively straightforward advice. By contrast, under the marital property system, ownership is not based on title but on asset classification; hence, the spouses may not understand (and cannot easily determine) who “owns” specific assets. *See supra* Chapter 2. Further, advice on the classification of assets requires factual and legal analysis, and each spouse has a right to independent professional judgment on his or her behalf regarding asset source, tracing, and classification questions. *See supra* Chapter 3. Whether joint representation is possible in various circumstances (especially in a second marriage with issue by a prior marriage) and whether an informed waiver of conflict of interest and a written consent to joint representation solve ethical concerns are matters to be considered. Another ethical concern may arise because of information received during a prior professional representation that the attorney is required to maintain in confidence.

**c. [§ 14.19] Marriage Agreements**

Under common law regimes, marriage agreements, other than premarital agreements, are uncommon. By contrast, under the Wisconsin marital property system, marriage agreements are more common and involve matters unique to that system (including classification of property, management rights, and credit). *See supra* Chapter 7. Marriage agreements may significantly affect property rights at death or divorce, and they are particularly common in connection with estate planning for clients with more substantial estates.

Determining the extent to which two independent attorneys are required in making these agreements and whether one may be the prior attorney for one or both spouses involves consideration of conflicts of interest and previously acquired confidential information. In addition, joint representation may affect the validity of the agreement itself under section 766.58(8). Section 766.58(8) states that if legal counsel is retained, the fact that both parties are represented by one attorney, or one party is represented by counsel and one is not, by itself is not sufficient to make a marital property agreement unconscionable or to affect its enforceability. Counsel should be wary of relying on this section for comfort in undertaking a joint

representation, especially if the agreement includes provisions that purport to affect property rights at divorce. *See infra* § 14.34.

#### **d. [§ 14.20] Management and Control**

Under Wisconsin marital property law, some rights of management and control exist independently of title, and the exercise of those rights can give rise to conflicts of interest between spouses. The lawyer advising spouses must be alert to these potential conflicts. *See supra* Chapter 4. When asked by a spouse for advice concerning the exercise of such rights, the lawyer must recognize that the advice may directly affect the interests of the other spouse, whom he or she also may represent, and may involve the duty of good faith under section 766.15 as well. These concerns generally do not exist under common law systems, because title is the determining factor in questions of management and control.

#### **e. [§ 14.21] Estate Planning**

The process of advising spouses on their estate plans gives rise to significant ethical considerations. The analysis must begin with the general rule that each spouse is entitled to independent advice concerning the ownership of assets, the control over assets at death, the options available to the spouse, and the effect of proposed or existing provisions of the estate plan documents not only on the spouse's nonmarital property but also on his or her interests in marital property. Similar considerations relate to consents to beneficiary designations or gifts, tax consequences of various actions (which may be adverse to one or the other spouse), and reclassifications of assets. *See supra* Chapter 10. Although the same ethical considerations exist under common law systems, those systems involve relatively straightforward spousal elective rights and ownership of property, in comparison to the many complex issues raised by a community property system. Hence, under a common law system, if a plan is developed by joint involvement or understanding, ethical considerations generally permit joint representation, with a relatively simple explanation of each document and its effect.

In planning estates involving Wisconsin marital property, if joint representation is used, the spouses' joint participation in the total process is necessary, including participation at the stages of analysis and decision making. The lawyer must be alert to the marital property interests of each

spouse and the possibly varying intentions of each spouse. *See* 1 R. Wilkins, *Drafting Wills and Trust Agreements (A Systems Approach)* 82 (1983); *see also* Bruce, *supra* note 5.

## 2. [§ 14.22] Conclusion

One approach to the preceding concerns is to conclude that each spouse must have separate counsel in matters involving his or her property. This approach rests on the general proposition that it is an attorney's responsibility to assert (or to advise independently, with undivided loyalty, of the possibility of asserting) those positions that are in the client's interest or for the client's economic or other benefit. Under this approach, assertions on behalf of one spouse concerning marital property could be contrary to the other spouse's interest. *See supra* section 14.4.

Some may argue that the spouses' situation in connection with marital property is analogous to the classic conflicts of interest between buyer and seller, injured party and alleged tortfeasor, or plaintiff and defendant in a lawsuit. However, spouses' circumstances need not be so characterized, and when appropriate and under the procedures outlined in this chapter, it may be ethical for one lawyer to advise and represent both spouses regarding their respective rights in marital property.

Whether it is ethical for one lawyer to advise both spouses in a specific situation depends on the lawyer's determination, based on the Rules of Professional Conduct for Attorneys (discussed at § 14.7, *supra*) and related guidance (including the factors listed in § 14.5, *supra*), of whether joint representation is practical, is in the interests of the clients, and is consistent with the lawyer's ethical duties, including the lawyer's duty to make professional services available on a cost efficient basis and the lawyer's role in accommodating differing interests. The answer also depends on the lawyer's ability to analyze the spouses' circumstances and explain to the spouses, in neutral terms, the legal and practical considerations involved in the matter. If the spouses then give informed, written consent to the joint representation, the lawyer may proceed (note, however, that not every joint representation of spouses necessarily involves a conflict that must be waived via a written consent; *see supra* § 14.10, citing the Restatement).

The lawyer must, however, be alert to changes in the relationships between the spouses and be willing to continually weigh the factors involved. If the factors or other significant circumstances change, the

attorney must reevaluate the basis for the joint representation. If this evaluation reveals that continuation of joint representation is not in the interest of each spouse, the attorney should bring that to the spouses' attention and withdraw if necessary. Conversely, if separate representation initially was required, and the factors or other circumstances change, the matter should be reevaluated and consideration given to whether joint representation thereafter may be appropriate or permissible.

#### **F. [§ 14.23] Ethical Responsibilities When Representing Only One Spouse**

When an attorney represents only one spouse, that spouse is the attorney's client, and his or her loyalty is to that spouse. Nonetheless, the attorney must be alert to and consider the duties and responsibilities his or her client has to the other spouse and the nature of their marital and nonmarital property. These factors are affected significantly by Wisconsin marital property law. The ethical duty of competency under SCR 20:1.1 requires the attorney to become knowledgeable and proficient in these matters. Marital property is a form of co-ownership between spouses, a duty of good faith exists between spouses, management and control of marital property by one spouse extends to property owned by the other spouse, and credit transactions by one spouse can affect the marital property interest of the other spouse. *See supra* Chapter 5 (credit transactions). But despite the partnership theory underlying Wisconsin's marital property system, the spouses remain two independent persons, each having independent legal capacity to act and enter into financial and other transactions. *See* Wis. Stat. §§ 765.001(2), 766.97. The Wisconsin marital property law does not impose any independent responsibilities on the attorney regarding the spouse whom the attorney does not represent, beyond those general responsibilities already imposed by the law governing lawyers, such as not participating in fraud.

As in other matters involving more than one party, especially parties having good faith obligations toward each other, the attorney who represents one spouse must be alert to the possibility that the other spouse may assume that the attorney also represents him or her.<sup>34</sup> To avoid this,

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<sup>34</sup> A critical ethical question for attorneys representing a spouse or spouses, and one not answered by the Rules of Professional Conduct for Attorneys, is "who is the client?" *See* Developments, *supra* note 5.



the attorney should make the extent of his or her representation clear to both spouses and (especially when the other spouse needs counsel or may rely on the attorney's advice to the client-spouse) encourage the other spouse to seek independent counsel. *See generally* SCR 20:4.3 (dealing with unrepresented person). Alternatively, assuming that the client-spouse concurs, the attorney may consider joint representation in accord with the considerations outlined in this chapter.

A few examples that illustrate the ethical responsibilities involved in representing only one spouse may be helpful. In each case, it is assumed that the attorney represents only one of the spouses, the attorney has not previously represented the other spouse, and there is no reasonable basis for the other spouse to conclude that the attorney represents him or her.

- **Example 1.** The client wife asks the attorney to assist in the sale of securities that are registered in her name alone, or in her name *or* her spouse's name (the alternative form). The attorney knows that the funds used to purchase the securities were derived from the spouses' income or earnings during marriage while Wisconsin residents, after the spouses' determination date, and that the securities are therefore marital property. Although each spouse has a marital property interest in the securities, the attorney has no duty to inform the other spouse before or after the transaction. Depending on the circumstances and the extent of the duty of good faith under section 766.15, the attorney may need to advise the client that she should or must do so. Under the management and control rules, the client spouse has the right to sell the securities. *See supra* Chapter 4.
- **Example 2.** The client husband requests advice and assistance in obtaining a purchase money mortgage loan to purchase investment real estate and in establishing a substantial line of credit. Among other things, the husband wants advice and assistance in preparing a financial statement that will list all marital property and each spouse's income. The equity in the real estate is to come from savings derived from the spouses' income and held in a marital account in a financial institution. For the same reasons as under example 1, the attorney has no duty to inform the other spouse before or after the transaction, even though the nonclient spouse's property interests may be subject to liability on the debt. Depending on the circumstances and the extent of the duty of good faith under section 766.15, the attorney may need to advise the client that that he should or must do so.

- **Example 3.** The client wife holds a high-yielding, insured, cash management fund account that is marital property. She asks for advice on investing all the account in a highly speculative venture with no prospect of income for a number of years. The attorney counsels the wife concerning the duty of good faith. For purposes of this example, it is assumed that the new investment would violate her duty of good faith to her husband but would not rise to the level of fraud. The attorney recommends that the wife obtain her husband's consent before proceeding in order to avoid a claim for breach of the good faith duty under section 766.70. The wife refuses to follow this advice. The duty of good faith under section 766.15 is a duty owed by each spouse to the other and does not create for the attorney an independent ethical responsibility to the nonclient husband. The attorney may continue to represent the wife and assist with the change in investment if she requests. The attorney has fulfilled his or her obligation by advising his or her client, and in fact, it would breach his or her duty of confidentiality to the client to reveal the transaction to the client's husband.<sup>35</sup>
- **Example 4.** The client husband wishes to make gifts of \$10,000 of marital property cash to each of his brother and his brother's wife, who have a financial emergency. For purposes of this example, it is assumed that the gifts would exceed the threshold amount in section 766.53 regarding gifts of marital property to third persons. The attorney advises the client to obtain his wife's consent to avoid the wife having a remedy against the husband and donees under section 766.70. The client husband refuses to follow this advice. Sections 766.53 and 766.70 create rights between the spouses and between the nonconsenting spouse and the donee, but do not create for the attorney an independent ethical responsibility to the nonclient.

The conclusions in these four examples apply despite a possible argument that, based on the nature of the spouses' marital property interests, the attorney is responsible to the nonclient spouse. For example, upon motion by the wife in a divorce action, the California intermediate appellate court disqualified the attorney for the family corporation from representing the husband. *Woods v. Superior Court*, 197 Cal. Rptr. 185 (Ct. App. 1983). Although the court did not mention it, the stock of the

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<sup>35</sup> The answer would be different if the transaction constituted fraud that the lawyer reasonably believed was likely to result in substantial injury to the financial interest or property of the husband. SCR 20:1.6(c)(1).

family corporation was owned by the spouses as community property. Letter From Attorney Arthur C. Kralowec to author (Sept. 10, 1985) (on file with author). The disqualification was based, in part, on the fact that a critical issue between the parties involved the valuation and related aspects of the corporation. It appears, however, that the court was strongly influenced by other unique facts, including the following: the wife had moved to join the corporation as a party; the attorney had previously represented the wife in preparing her will; the wife had consulted the attorney concerning the value of the business and the family home; the wife alleged that she had consulted with and had obtained the attorney's advice concerning the spouses' marital discord; and the court's finding that it was likely that the attorney would be called as a witness. Regardless of the nature of the ownership of the stock, absent the wife's consent, the attorney was properly disqualified under these facts. *See supra* §§ 14.8–.12.

However, the decision contains language, arguably dicta, indicating the court's view that representation of a family corporation may be sufficient to bar representation of one of the spouses in litigation in which the corporation is a critical element. *Woods*, 197 Cal. Rptr. at 189. In all events, in a nonlitigation context, such as discussed in the above four examples, the co-ownership of marital property, such as stock in a family corporation, does not provide a basis for a direct duty to the nonclient spouse. Further, in the context of divorce litigation, absent unique facts such as in *Woods*, representation of a corporation whose stock is owned by the spouses as marital property should not disqualify an attorney from representing one spouse against the other spouse who the attorney has not previously represented.

In State Bar of Wisconsin Standing Committee on Professional Ethics, Formal Opinion E-88-12 (1988) (Simultaneous Representation of Corporation and Corporate Officer), the committee determined that a lawyer who represents a closely held corporation in which A is the sole stockholder may also represent A in a divorce action, even if A's spouse has a marital property interest in the stock. For a criticism of this opinion, as well as further discussion of *Woods*, see *Ethics and Dual Representation*, L. Marital Prop. F., May 1989, at 2; but see *Ethics and Dual Representation Revisited*, L. Marital Prop. F., Nov. 1989, at 4, for a response supporting the rationale of this ethics opinion and asserting that, consistent with the text of this section, there should not be an automatic finding of impermissible conflict and disqualification in this and in similar situations.

The above rationale is also supported by the Wisconsin Supreme Court's conclusion in *Jesse by Reinecke v. Danforth*, 169 Wis. 2d 229, 485 N.W.2d 63 (1992), in which the court applied the "entity rule." The court held that the lawyer who represented the corporation with respect to its formation, and also represented the individuals (who later became shareholders) in connection with pre-incorporation activities, was not disqualified from representing an unrelated third party in a lawsuit against two of the shareholders. The court concluded that the client was the corporate entity and not the individual shareholders and that services in connection with the incorporation (and advice with respect to corporate structure, etc.) for the prospective shareholders before the incorporation are deemed to be services for (and advice to) the corporation.

For a discussion of issues that can arise in representing one spouse in the context of a marital property agreement, see section 14.27, *infra*.

#### **IV. [§ 14.24] Application of Rules and Suggested Factors to Specific Joint Representation Situations**

##### **A. [§ 14.25] In General**

The facts of a particular case have a substantial bearing on ethical conclusions. Thus, the situations of joint representation discussed under this heading should be considered illustrative only and are not to be relied on as authoritative. They are intended to aid analysis of particular situations facing attorneys in the marital property setting.

In resolving ethical problems, the Rules of Professional Conduct for Attorneys and their application to the particular factual circumstances must be considered; additional guidance may be found in the comments following each rule. Further, in using this book, the factors and discussion in sections 14.2–.23, *supra*, should be considered before referring to the specific situations under this heading.

For additional views on applying the ABA model rules to particular factual circumstances, see the *ACTEC Commentaries*, *supra* note 10, and *Representing Husband and Wife*, *supra* note 5. See also Bruce S. Ross, *How to Do Right by Not Doing Wrong: Legal Malpractice and Ethical Considerations in Estate Planning and Administration*, 28 *The Annual Phillip E. Heckerling Institute on Estate Planning* ch. 8 (1994); Hazard, *supra* note 13; references cited at sections 14.4–.5, *supra*.

## **B. [§ 14.26] Marital Property Agreements**

### **1. [§ 14.27] General Marital Property Agreements**

From an ethical perspective, the general rule of thumb is that each party to a marital property agreement, especially a premarital agreement, should be represented by independent counsel.

The hazards inherent in representing a spouse (or a person about to enter marriage) with respect to a marital property agreement (particularly when an attorney's actions are judged with the benefit of hindsight) are well illustrated by the case of *Estate of Campbell v. Chaney*, 169 Wis. 2d 399, 485 N.W.2d 421 (Ct. App. 1992). In that case, the attorneys represented the future husband in preparing a premarital agreement containing a waiver of the elective share of the wife-to-be. The validity of the agreement was challenged after the husband's death by his widow, who sought to receive her elective share from his estate rather than a lower amount prescribed by the premarital agreement.

The estate settled with the widow and brought a malpractice action against the attorneys who represented the husband, claiming that their negligence in drafting the agreement allowed the widow to assert her claim and caused the estate to settle with her. The issue on appeal was whether the estate would have to prove that it would have lost in the widow's lawsuit, in which case a "trial within a trial" would be required. The court of appeals held that a trial within a trial was not necessary and that the estate would not have to prove that it would have lost such a lawsuit in order to recover any loss (cost of litigation and amount paid to settle her claim) resulting from the widow's claim.

The court held that the issue was not the validity of the premarital agreement, but whether the attorneys' alleged negligence forced the estate to engage in litigation in which it otherwise would not have been involved. This, in turn, would depend on whether the attorneys failed to live up to the requisite standard of care in preparing the premarital agreement and whether such negligence (if found) "caused weakness" in the agreement that caused the widow's claim. Of course, the estate also would be required to demonstrate that the settlement it reached was reasonable and made in good faith. *Id.* at 409–10.

The difficulties faced by an attorney who represents one party to a marriage agreement when the other party is not represented are illustrated by *In re Marriage of Foran*, 834 P.2d 1081 (Wash. Ct. App. 1992). This

case involved a premarital agreement that was held, as a matter of law, to be unreasonable and economically unfair to the wife, who had been unrepresented. As a result, under Washington law, the burden was placed on the husband, who had been represented, to establish that the agreement had been entered into by the wife voluntarily and with full knowledge of her rights. In fact, the evidence indicated that the agreement was (1) the result of duress; (2) presented to the wife nearly on the eve of marriage; and (3) presented to the wife with only general information as to its effect.

On the day the agreement was signed, the husband's lawyer delivered to the parties the draft of the agreement and an explanatory letter. The letter confirmed that the lawyer solely represented the husband and that, if the wife had questions regarding her rights or the legal import and effect of the agreement, she should seek separate counsel solely on her behalf.

The Washington court stated that when a premarital agreement is economically unfair, its enforcement requires proof that each party entered into the agreement voluntarily and *intelligently*. In this case, the court concluded that the wife had not entered into the agreement intelligently, since it was not established that she fully understood its legal consequences (i.e., that it was economically unfair). The attorney's general letter, written at the last moment, was insufficient to satisfy this test. The attorney did not explain to the unrepresented spouse why it was so important to seek advice from separate counsel (in this case, according to the Washington court, for the purpose of assisting the wife in negotiating an economically fair contract and to explain clearly the economic effects of the agreement). The court in no way implied, however, that the attorney had not lived up to his ethical responsibilities, including those regarding the potential conflict of interest.

It should also be noted that Washington's tests for validity and enforceability of a marriage agreement are different from Wisconsin's tests. Accordingly, the case is not instructive regarding Wisconsin law. See section 7.14, *supra*, regarding the enforceability of marital property agreements, and section 7.14(a)(4), *supra*, regarding the effect of lack of separate counsel. Nonetheless, the *Foran* case provides insight with respect to some of the various ethical considerations involved and the possible precautions that may be indicated under some circumstances, with respect to the professional responsibilities of an attorney representing one spouse when the other spouse is unrepresented.

Other than divorce, the situation of spouses entering into a general marital property agreement is as inherently conflicting or antagonistic as can be found in the marital property setting. *See supra* § 14.22. However, consistent with the factors outlined in section 14.5, *supra*, and applying the rule of informed written consent following consultation, there are situations in which joint representation may be appropriate. In such cases, the attorney should exercise special caution regarding provisions that may affect property division or support in the event of a divorce. In addition, whenever a marital property agreement includes provisions relating to divorce (for example, property division or maintenance), joint representation is not appropriate except in the most unusual circumstances. Generally, each party should be represented by independent counsel. A spouse may elect not to be represented, but this may present an ethical problem for the attorney representing the other spouse. For further discussion, see section 14.34, *infra*.

When independent representation is indicated, another issue relates to the form or required extent of such representation. This issue can be particularly difficult when the representation arises after the discussion and drafting stages have been completed. For example, one attorney may have drafted a marital property agreement for the spouses, pursuant to their informed consent to joint representation. However, the spouses may then decide to include divorce provisions (or, for other reasons, joint representation may no longer be appropriate). At that point, each spouse needs independent representation. The spouses may consent to the original attorney's continued representation of one of the spouses, and the other spouse may engage a second attorney with the expectation that he or she will merely advise regarding the divorce provisions. What is the extent of the duty of the second attorney with respect to the proposed agreement as a whole? How vigorous must the second attorney's advocacy be in order to fulfill his or her duties in the representation?

Similarly, the spouses may agree that their attorney will represent only one of the spouses in the preparation of a marital property agreement and that, after it is prepared, the other spouse will take the agreement to another attorney who the spouses expect will simply review it on behalf of the other spouse.

The following illustrations provide examples of common factual situations involving general marital property agreements in which joint representation may be appropriate. In each, assume the agreement does not include provisions for the disposition of property at divorce.

1. First marriage for both parties, and both parties are employed in roughly equivalent positions, have approximately equal estates, and are knowledgeable and “independent.”
2. First marriage for both parties, and neither party has a significant estate; a “traditional” marriage is planned (with wife a stay-at-mother and husband as primary wage earner), neither party is more knowledgeable than the other, and the parties want all their property classified as marital property.
3. First marriage for both parties, and the parties share common goals and objectives with respect to their desire to provide for one another and ultimately for their children in a tax-efficient manner.
4. Second marriage for both parties, and each party has children from a prior marriage; each also has a separate estate, and although one estate is larger than the other, the difference is not substantial; in addition, both parties are knowledgeable and “independent,” and want their property to remain separate and pass to their respective children by prior marriage.

Assume that the attorney explains generally both the marital property system and the advantages, disadvantages, and implications of joint representation. After that, the parties ask the attorney to help them develop the agreement, and they provide written consent to the joint representation. In each of the examples above, if factors 1 through 9 in section 14.5, *supra*, or other facts do not tip the scale in favor of independent representation, joint representation would generally be ethically permissible. It is suggested that a confirming letter be sent to the clients, briefly summarizing the lawyer’s explanation, the parties’ request, and their respective consents. A sample letter, which should be tailored to each particular case, appears in section 14.35, *infra*.

While joint representation of spouses with respect to an agreement that contemplates the disposition of property at divorce is generally ill-advised, it will not necessarily render the agreement invalid. The New York Court of Appeals held, in a divorce action in which the spouses’ separation agreement was challenged on the basis of joint representation, that

[A]s long as the attorney fairly advises the parties of both the salient issues and the consequences of joint representation, and the separation agreement arrived at was fair, rescission will not be granted. While the potential conflict of interests inherent in such joint representation suggests that the husband and



wife should retain separate counsel, the parties have an absolute right to be represented by the same attorney provided “there has been full disclosure between the parties, not only of all relevant facts but also of their contextual significance, and there has been an absence of inequitable conduct or other infirmity which might vitiate the execution of the agreement.”

*Levine v. Levine*, 436 N.E.2d 476, 479 (N.Y. 1982) (citations omitted). The court ruled that the fact that the husband’s attorney represented both parties did not, without more, establish overreaching by the husband. The court emphasized that the trial court found that the attorney had remained neutral throughout his involvement (apparently, the parties had agreed on the essential terms before contacting the attorney).

It is significant that joint representation is contemplated by the Wisconsin Marital Property Act. Under the Act, the fact that one party is unrepresented or both are represented by one counsel does not by itself make the marital property agreement unconscionable or otherwise affect its enforceability. Wis. Stat. § 766.58(8); *see supra* § 7.14a(4). It should be emphasized that this statutory provision does not resolve the ethical questions,<sup>36</sup> but it appears to reflect a policy permitting, if not encouraging, joint representation in appropriate situations. When independent representation is waived, it is suggested that the waiver also be contained in the marital property agreement itself.

## **2. [§ 14.28] Limited Marital Property Agreements**

A marital property agreement between spouses may be used for limited as well as general purposes. *See supra* Chapter 7. Subject to considerations reflected in factors 1 through 9, *see supra* § 14.5, independent counsel may be needed less frequently for limited agreements. Often, the purpose of a limited agreement may be to accommodate a joint desire of the spouses, sometimes based on a decision arrived at independently of the lawyer. After analyzing the factors and applying the rule of informed consent, the lawyer may conclude that joint representation is appropriate. The following are examples of limited marital property agreement situations in which joint representation likely will be appropriate:

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<sup>36</sup> The Legislative Council supplemental note to 1985 Trailer Bill § 177m, amending § 766.58(8), is in accord. *See* Wis. Stat. Ann. § 766.58 Legis. Council Comm. Supplemental Notes Relating to 1985 Act 37 (West 1993).

1. Agreement to provide that income on presently owned marital or nonmarital property, and property traceable to that property, shall be individual property. Caution is indicated if this would cause substantial inequality between the parties or if the agreement covers future acquisitions (for example, assets acquired by the spouse by gift or inheritance), but joint representation may still be appropriate.
2. Agreement to provide that specific life insurance on the life of a spouse, not owned by one of the spouses (for example, owned by a child or trust), will not have a marital property component even if marital funds are used to pay premiums.
3. Agreement to provide that either spouse may freely name the beneficiary of specific life insurance or an employee benefit held by that spouse, with the other spouse waiving all marital or deferred marital property claim to it, even if the item has a marital property component.
4. Agreement to provide sole management and control of specific assets (or a class of assets) held by the spouses or by one spouse.
5. Agreement to reclassify an asset or a limited number of assets as the individual property of one of the spouses (for example, to permit specific bequests of that property or to facilitate estate tax planning).

*See also supra* § 14.27 (comments following illustrations).

### **C. [§ 14.29] Ownership; Management and Control**

Advising spouses regarding their respective ownership interests in property and their rights of management and control presents classic conflicts of interest. *See supra* §§ 14.15–.22. However, if the attorney does not have reason to believe that there is underlying hostility or conflict, and if the factors do not indicate the advisability of separate counsel, *see supra* § 14.5, the attorney may proceed to give advice and perform professional services if the spouses consent under the procedures discussed in section 14.11, *supra*.

In the joint representation situation involving ownership or management and control of marital property, even though written consent is given, it is important that the attorney keep both spouses informed of the advice given to either of them, because the advice to one probably will affect the other. If a spouse to whom advice is given insists that this information not be

conveyed to the other spouse and proceeds with the contemplated action, the attorney may be forced to withdraw as counsel for both spouses (unless the other spouse consents to the attorney continuing to serve as counsel for the advised spouse). *See supra* § 14.12. An appropriate letter of consent to joint representation, *see supra* § 14.11, waiving confidentiality between the spouses, would effectively avoid this problem. However, the letter is revocable prospectively by either spouse, and each remains free to obtain independent counsel at any time. It appears that, in a joint representation situation, one spouse's insistence that information not be conveyed to the other spouse, as described above, may amount to a revocation of that spouse's waiver of confidentiality and his or her consent to joint representation. *See supra* § 14.11, *infra* § 14.32.

A consent to joint representation should be current. A "blanket" consent, covering *all* future transactions, without more, is not sufficient. However, it does not seem to be necessary to obtain a new consent for each possible conflict of interest within a general area for which consent previously has been given. A rule of reason applies, and continuing consent may be implied by the course of dealing with the spouses. On the other hand, if a new matter arises involving considerations not related to the original explanation and consent, the lawyer should explain the new considerations to the spouses and obtain a new informed consent. In that instance, it is advisable to send a letter to the spouses, obtaining their written confirmation of continuing consent. If new conflicts of interest arise, involving substantial matters and differing considerations, a new written consent by the spouses would be required. *See supra* § 14.12.

In sum, joint representation creates for the attorney a continuing duty to disclose to the clients subsequent developments that might affect the attorney's independent judgment and the spouses' prior consent. *See* Annotated Code, *supra* note 19, at 243–44.

#### **D. [§ 14.30] Credit Transactions**

The considerations involved in representing spouses in ownership and management and control situations, *see supra* § 14.29, also apply to credit transactions. In addition, in nearly all unilateral credit transactions by a spouse, there is an immediate economic effect (advantageous or detrimental) on the other spouse and the marital property of the spouses. Differing interests, if not direct conflicts of interest, may be inherent in credit transactions. For example, a credit transaction by one spouse that creates

an obligation in the interest of the marriage or family exposes to creditors all marital property of the spouses, including the other spouse's income. *See supra* Chapter 5. Further, a spouse is required to act in good faith with respect to the other spouse in credit transactions involving marital property. *Id.*

Accordingly, if the attorney represents both spouses (except when the joint representation has concerned an unrelated transaction), it is advisable that the other spouse be informed of professional services or advice rendered to one spouse. Under joint representation, unless the other spouse has consented in writing in advance to the particular representation relating to credit, the attorney should advise the other spouse before proceeding.

### **E. [§ 14.31] Personal Injury Litigation**

Various conflicts of interest may arise in connection with personal injury accident claims and the litigation or settlement of those claims. For example, the question of the allocation of recovery involves a potential conflict if damages are sought for both loss of income and pain and suffering. Under section 766.31(7)(f), a recovery for personal injury is individual property except that portion attributable to expenses paid or otherwise satisfied with marital property and except for the amount attributable to loss of income during marriage. As a result, a conflict can arise in negotiating a settlement, structuring a settlement, and developing the theory and presentation of the case, as well as in other instances.

An attorney who represented both spouses before the accident and is asked to represent the injured spouse, or an attorney who is asked to represent both spouses with or without any prior representation, should be alert to these and related conflicts. The attorney should proceed with joint representation only after concluding that he or she may adequately represent both spouses under the guidelines of SCR 20:1.7 (*see supra* § 14.11) and after concluding that none of the factors in section 14.5, *supra*, or any other fact points to the necessity of independent representation. It is recommended that the attorney send a letter to the spouses, summarizing the attorney's explanation and giving the parties the opportunity to request in writing that the attorney serve, with such writing to contain their respective consents. Such a letter can be modeled after the sample letters in sections 14.35–.36, *infra*.

## F. [§ 14.32] Estate Planning

Estate planning represents an ideal situation for joint representation, particularly because of the advantages of coordinated planning, the promotion of harmony, and the efficiencies that can be obtained by the use of one attorney for both spouses. Nevertheless, the attorney must be alert to the potential ethical problems, particularly those that may arise as the planning progresses.<sup>37</sup> It also should be noted at the outset that the conflict-of-interest rules under SCR 20:1.7 were intended to deal with parties in directly adversarial situations, such as in litigation, and not with estate planning (and related areas such as probate and trust administration). *See supra* § 14.8; *see also* Developments, *supra* note 5, at 2; Bruce, *supra* note 5 (discussion and sample joint representation letters); *supra* §§ 14.4–.12 (additional references).

The general principles outlined in sections 14.2–.14, *supra*, apply to estate planning. However, unless an acrimonious relationship exists or the factors discussed in section 14.5, *supra*, point to the necessity of independent counsel, one attorney may represent both spouses in developing their estate plan, preparing the documents, and implementing the plan. The situation is no more inherently conflicting than some of the others described above, *see supra* §§ 14.26–.31, but because the estate planning process involves disposition of all of a spouse's assets, significantly affects each spouse's interest in marital property, and may affect each spouse's credit, special care is required.<sup>38</sup>

If, after the attorney has generally explained the marital property system, the estate planning process, the spouses' respective rights, and the advantages and disadvantages of joint representation, the spouses ask the attorney to proceed on their joint behalf and consent in writing to joint representation, there is no reason why the attorney cannot represent both spouses. This assumes, of course, that the attorney has concluded that the matter is appropriate for joint representation. *See supra* §§ 14.5–.12. For spouses who are existing pre-Act estate planning clients, the explanation may be less extensive, but not with respect to the marital property system and the spouses' respective rights.

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<sup>37</sup> *See* Flaherty, *Conflicts of Interest Arising in the Two-Spouse Estate Planning Context*, Est. Gift & Tr. J. 17, 20 (1982).

<sup>38</sup> *See* James R. Wade, *When Can a Lawyer Represent Both Husband and Wife in Estate Planning?*, Prob. & Prop., Mar./Apr. 1987, at 12.

The following ethics opinion succinctly states the ethical considerations involved and the propriety of proceeding in this manner:

A lawyer may represent both husband and wife in estate planning matters provided the lawyer makes full disclosure of the possible effect of this multiple representation on the exercise of his independent professional judgment on behalf of each client, explaining in plain English the meaning and personal impact of the plans ultimately crafted. The clients should be willing to waive their rights of having the lawyer guard each client's confidence. The lawyer should be authorized to disclose all the assets involved to each party, as well as to disclose the terms of each will. Whether the lawyer conducts this business in separate or joint meetings does not matter so long as he makes full disclosure. Since one spouse more likely holds the bulk of assets and will probably pay the lawyer, the lawyer should exercise care not to permit this spouse to regulate or distort his judgment. While the potential for conflict exists between the husband and wife, they may seek one lawyer as a problem solver, not as an advocate, with the expectation that they may have to accept compromises for the overall advantage of the family.

Allegheny County (Pa.) Bar Ass'n Prof. Ethics Comm., Op. (Mar. 1, 1983) (reprinted in ABA/BNA Manual (Ethics Opinion, 1980–85), *supra* note 17, at 801:7401–:7402).

Because of the complexities of marital property and the additional areas of potential conflict and divergence of interest, it is suggested that either before, at, or soon after the initial estate planning conference, the attorney should send an explanatory letter to the spouses, confirming the consultation and requesting the spouses' written consent. *See* SCR 20:1.7 ABA cmt. (Consultation and Consent). A sample letter, which requires tailoring in each instance, appears in section 14.36, *infra*. The letter follows the general format of the suggested letter in Flaherty, *supra* note 37.

Questions may arise over whether, after performing estate planning services for both spouses, an attorney may thereafter draft inconsistent planning documents for one of the spouses. The general rule is that he or she may not, absent an informed, written consent, but requesting such consent may not be possible because the attorney could then violate the confidentiality rules of model rule 1.6 (SCR 20:1.6). *See supra* §§ 14.7–.13. This situation was illustrated by the following opinion of the Ethics Committee of the State Bar of Arizona:

Lawyer A drafts separate wills for Mr. and Mrs. X, both of which contain substantially the same clauses by which both leave their property to each other. Both Mr. and Mrs. X are aware of the contents of each will. Later Mrs. X

comes to A and wants to have her will changed so that all of her property would be left to her children. Although Mrs. X may, of course, dispose of her property as she sees fit, and although Mr. X has no legal right in her property, A would be diluting his loyalty to Mr. X if he made the change in Mrs. X's will. He should not do that and should not inform Mr. X of the proposed change.

State Bar of Ariz. Comm. on Rules of Prof. Conduct, Op. 76-15 (Aug. 10, 1976). *See also supra* § 14.13 (discussion of Florida Ethics Opinion 95-4).

This situation, involving the completion of a coordinated estate plan for the spouses and a later change in one spouse's desires, places the lawyer in a dilemma. Assuming that the above facts involve continued joint representation, the Arizona ethics opinion seems correct in proscribing the lawyer from preparing the inconsistent will or codicil. However, if there is prior consent to joint representation, and one spouse requests the attorney to prepare a new inconsistent will or codicil, the lawyer should be permitted to inform both parties that one spouse has asked the lawyer to prepare a change that is inconsistent with the coordinated plan. The lawyer should then explain that he or she cannot proceed without consent being renewed by both spouses.

The rule has been succinctly stated as follows: "When the interests of clients diverge and become antagonistic, their lawyer must be absolutely impartial between them, which, unless they both or all desire him to represent them both or all, usually means that he may represent none of them." Drinker, *supra* note 7, at 112. For example, if two persons for whom an attorney prepared a contract or mortgage become involved in a dispute concerning the contract or mortgage, the lawyer may not be able to represent either in the dispute. *Id.* at 113. However, in the spousal context, with appropriate consent, the attorney may possibly represent one spouse in the dispute. *See supra* §§ 14.12, .23; *see also* State Bar of Wis. Standing Comm. on Prof. Ethics, Formal Op. E-83-9 (1983) (Attorney's Obligation When Clients Develop Adverse Interest).

The attorney should be alert to other areas of potential conflict in the estate planning context and explain them to the spouses as the estate planning proceeds. *See Developments, supra* note 5, at 10. Among these other areas are the following:

1. Classification of property, including deferred and terminable interest marital property;

2. Consents for beneficiary designations, including gift tax aspects;
3. Effect of transfers to revocable trusts;
4. Selection of fiduciaries (and attorneys, if appropriate);
5. Classification of debts and directions for payment;
6. Forced and voluntary elections; and
7. Will substitute marital property agreements (Washington wills).

An attorney preparing a will for his or her spouse and naming the attorney or a person related to him or her as beneficiary presents another ethical issue in estate planning. The rule for this situation is found in SCR 20:1.8(c), which provides:

A lawyer shall not prepare an instrument giving the lawyer or a person related to the lawyer as parent, child, sibling, or spouse any substantial gift from a client, including a testamentary gift, except where:

- (1) the client is related to the donee,
- (2) the donee is a natural object of the bounty of the client,
- (3) there is no reasonable ground to anticipate a contest, or a claim of undue influence or for the public to lose confidence in the integrity of the bar, and
- (4) the amount of the gift or bequest is reasonable and natural under the circumstances.

Prior to a 1991 amendment to SCR 20:1.8(c) by the Wisconsin Supreme Court, paragraph (4) of the rule further required that the bequest to the lawyer could provide no more than the lawyer would receive under the laws of intestacy. With the exception of that change, SCR 20:1.8(c) is based on the decisions of *State v. Collentine*, 39 Wis. 2d 325, 159 N.W.2d 50 (1968), and *State v. Beaudry*, 53 Wis. 2d 148, 191 N.W.2d 842 (1971). *See also State v. Gulbankian*, 54 Wis. 2d 599, 196 N.W.2d 730 (1972); State Bar of Wisconsin Standing Committee on Professional Ethics, Formal Opinion E-80-1 (1980) (Drafting Will for Partner's Spouse) (applying rule that disqualification of one lawyer in an organization generally disqualifies all affiliated lawyers).

With regard to the common representation of husband and wife in estate planning matters, see generally *ACTEC Commentaries*, *supra* note 5; *Representing Husband and Wife*, *supra* note 13; *see also supra* §§ 14.4–.5. With regard to client confidence issues in representing a husband and wife in estate planning matters, see the discussion at section 14.13, *supra*. On



the subject of representation of multiple clients in the estate planning context, see *In re Estate of Koch*, 849 P.2d 977 (Kan. Ct. App. 1993), discussed at section 14.5, *supra*. For a discussion separate versus joint representation generally see section 14.4, *supra*.

### **G. [§ 14.33] Probate**

The attorney serving as counsel for the personal representative must be alert to normal conflicts of interest plus those inherent in the probate process and the representation of a fiduciary.

These have been heightened by the adoption of the marital property system. The general considerations outlined in sections 14.2–.14, *supra*, apply, but in some circumstances the factors tending to favor joint representation may not apply or may not be persuasive. Further, the rules of consent may not be practical in view of some of the fiduciary relationships. In such instances, independent representation may be required.

The following five illustrations offer some guidance.

1. Independent personal representative (who is not the spouse); surviving spouse is the sole beneficiary of the estate (or the only other beneficiaries are beneficiaries of pecuniary or specific bequests that can be satisfied without regard to questions of classification of assets or debts). In this case, the attorney for the surviving spouse may serve as attorney for the personal representative, and consent is not required because no conflicts of interest appear. Note, however, that if a dispute were to arise between the personal representative and the surviving spouse, the attorney would need to withdraw from representation of both (at least with respect to the issue in dispute), or with the consent of both parties represent only one of them with respect to such issue.
2. Independent personal representative (who is not the spouse); surviving spouse is not the sole beneficiary of the estate (spouse owns his or her one-half interest in the former marital property, but, for example, the residue of the estate passes in trust for the decedent's children). In this scenario, the attorney for the surviving spouse probably should not serve as attorney for the personal representative without the consent of the personal representative and the surviving spouse. (Further, the lawyer may have a duty to advise the personal representative to seek approval of the interested persons before consenting to the representation.) The primary reason is that it is the personal representative's duty

to assert classification of individual property rather than marital property and to assert other positions conflicting with the surviving spouse's interest. It should be noted that the responsibilities regarding classification are vested in the personal representative and not the attorney. If a specific conflict arises between the personal representative and the surviving spouse, separate representation may be required, and the attorney may not represent either party without the consent of both. If the surviving spouse obtains independent counsel, the original attorney for the surviving spouse still should not represent the personal representative without the spouse's consent. The results suggested in this paragraph may be different if the spouses have entered into a marital property agreement which clearly delineates what marital property rights exist.

3. The attorney represented the spouses during the decedent's lifetime and is appointed personal representative under the deceased spouse's will; the surviving spouse is not the sole beneficiary of the estate. It appears that in this case, the attorney may serve as personal representative, attorney for the estate, and attorney for the surviving spouse (despite the fact that the attorney, as personal representative, must exercise independent judgment regarding classification of property, payment of debts and expenses, and so on), because the decedent created the apparent conflict, and the persons interested are free to challenge such exercise. If, however, a conflict arises and a challenge is made, the attorney may not serve as attorney for the surviving spouse, and independent representation is required.
4. Independent personal representative (who is not the spouse); in this situation, the attorney who prepared the decedent's estate plan, but did not represent the decedent's spouse, may represent the personal representative. If all the assets pass to the surviving spouse, or there are no questions concerning marital or deferred marital property, the attorney also may represent the decedent's spouse with regard to his or her interest in the estate, without approval of the personal representative.
5. The surviving spouse is not the sole beneficiary of the estate; the surviving spouse is appointed personal representative under the decedent's will. In this case the surviving spouse's attorney may serve as attorney for the personal representative. The surviving spouse (and hence, his or her attorney in each capacity) has a conflict of interest between his or her duty as personal representative to assert classifica-

tions of property that will enhance the probate estate, and his or her personal interest to assert the contrary with respect to marital and individual property. However, since the decedent presumably knew of the potential conflict, and the personal representative is free to select his or her own counsel, the attorney may proceed with representation unless an actual conflict arises.

In connection with probate, in addition to the considerations outlined in sections 14.2–14, *supra*, and this section, the attorney should be alert to other areas of potential conflict. Among these are the following:

1. Classification and collection of property, and asserting individual or marital interests therein;
2. Use of presumptions, and possibly not attempting to rebut them if advantageous to the estate;
3. Treatment of property passing independent of probate;
4. Validity and effect of marital property agreements, consents, and waivers by the decedent;
5. Violation of good faith duty by the other spouse;
6. Forced and voluntary elections; and
7. Payment of debts and expenses.

For further discussion, see Developments, *supra* note 5.

For a thorough discussion of the various ethical issues and dilemmas facing the lawyer for a fiduciary in the trusts and estates context, see *Counseling the Fiduciary*, a report of the Special Study Committee on Professional Responsibility of the Section of Real Property, Probate and Trust Law of the American Bar Association, *reprinted at* 28 Real Prop. Prob. & Tr. J. 825 (1994); *see also* Robert W. Tuttle, *The Fiduciary's Fiduciary: Legal Ethics in Fiduciary Representation*, 1994 U. Ill. L. Rev. 889 (1994); ABA Standing Committee on Ethics and Professional Responsibility, Formal Op. 94-380 (1994) (Counseling a Fiduciary), the summary of which states as follows:

A lawyer who represents the fiduciary in a trust or estate matter is subject to the same limitations imposed by the Model Rules of Professional Conduct as are all other lawyers. The fact that the fiduciary has obligations to the beneficiaries of the trust or estate does not in itself either expand or limit the lawyer's

obligations to the fiduciary client under the Model Rules, nor impose on the lawyer obligations toward the beneficiaries that the lawyer would not have toward other third parties. Specifically, the lawyer's obligation to preserve the client's confidences under Rule 1.6 is not altered by the circumstance that the client is a fiduciary.

Both the *ACTEC Commentaries*, *supra* note 10, and the report *Counseling the Fiduciary* take a more expansive approach on the subject of disclosures by the lawyer for the fiduciary. For example, the Commentary on Model Rule 1.6 states: "[T]he fiduciary's retention of the lawyer to represent the fiduciary generally in the administration of the fiduciary estate may impliedly authorize the lawyer to make disclosures in order to protect the interests of the beneficiaries." The report *Counseling the Fiduciary* describes various circumstances under which duties may arise to beneficiaries even where the lawyer represents only the fiduciary.

## H. [§ 14.34] Divorce

Each spouse should be separately represented in divorce proceedings. Although there is a contrary view that it may be appropriate to represent both spouses in no-fault divorce proceedings (based on the philosophy that one should not create a controversy between parties when none exists), *see Annotated Code*, *supra* note 19, at 238 (citing *Klemm v. Superior Court*, 142 Cal. Rptr. 509 (1977)), the prudent rule is stated by the March 25, 1983, Opinion of the Ethics Committee of the Mississippi State Bar (published after submission to the bar's board of commissioners):

An attorney may not represent both parties in a no-fault divorce. The interests of the parties are conflicting, inconsistent, diverse, and otherwise discordant, no matter what the parties themselves believe. Serving one client's interest may result in not adequately representing the other client's interest. The lawyer's loyalty will be divided.

ABA/BNA Manual (Ethics Opinions, 1980–85), *supra* note 17, at 801:5104–:5105.

A formal opinion in Wisconsin based on ABA code canon 5 flatly holds that an attorney may not represent both spouses in a divorce proceeding. State Bar of Wis. Standing Comm. on Prof. Ethics, Formal Op. E-84-3 (1984) (reprinted at 57 Wis. Bar Bull. 40, 88 (June 1984)). Former Wisconsin Supreme Court Rule 20.23(3)(b) (EC 5 15) stated that "A lawyer should never represent in litigation multiple clients with differing

interests . . . .” In the committee’s opinion, divorce under chapter 767 is litigation, whether contested or uncontested, and divorcing spouses have differing interests (even if they appear to be in agreement, since the probabilities of unrevealed differing interests remain high), and therefore joint representation is improper.

Another formal opinion, State Bar of Wis. Standing Comm. on Prof. Ethics, Formal Op. E-79-2 (1979) (reprinted at 57 Wis. Bar Bull. 40, 61 (June 1984)), disapproved of a proposed agreement between a lawyer and a married couple considering divorce under which the lawyer proposed to mediate disputes arising in the course of settlement negotiations. The committee concluded that under the facts of the opinion, such a role was unethical because the lawyer would be serving as legal counsel for the parties, which placed the lawyer in an unresolvable position of conflict in view of the adversarial nature of divorce proceedings. However, Formal Opinion E-79-2, which predated Wisconsin’s adoption of model rule 2.2, was subsequently withdrawn by Formal Opinion E-97-3, which states that “An attorney may serve as an intermediary between two current clients, such as a husband and wife in a divorce action, if the requirements of SCR 20:2.2 are met. . . .”<sup>39</sup>

The Wisconsin Marital Property Act does not affect the Family Code itself, but the Act’s added complexities relating to ownership of property, credit transactions, good faith duty, interspousal remedies, and the like emphasize the necessity of separate representation for each spouse in an action for divorce or related relief.

Consistent with the principle that each spouse should be separately represented in a divorce proceeding, one lawyer should not represent both spouses in connection with a marital property agreement that includes provisions for property division or maintenance in the event of dissolution of the marriage. Section 767.255(3)(L) provides that a written agreement by spouses or parties intending to be married “concerning any arrangement for property distribution” is a factor to be considered by the court in

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<sup>39</sup> To summarize, a lawyer should not undertake a joint representation of spouses in a divorce proceeding, but a lawyer may serve as an intermediary in resolving disputed issues if the requirements of SCR 20:2.2 are met. Note that the new ABA model rules (currently under consideration in Wisconsin—see discussion at section 14.9, *supra*) do away with model rule 2.2 and incorporate its requirements into model rule 1.7 (for client representations) and a new model rule 2.4 (specifically for mediation).

determining the property division at dissolution. The statute also provides that such an agreement is binding upon the court unless the terms are inequitable as to either party. In addition, section 767.26(8) provides that agreement concerning financial support is a factor to be considered by the court in determining maintenance payments. Since advice and representation concerning such provisions may involve conflicts of interest, *see supra* § 14.8, and ultimately may involve divorce proceedings, joint representation is inappropriate except in the most unusual circumstances. From the standpoint of litigation, moreover, such provisions may be viewed as in the nature of a stipulation, for which independent counsel would be required.

A recent trend may represent a caveat to the above general principles. “Collaborative divorce” has received a significant amount of attention in Wisconsin. The concept is that each spouse is independently represented, but the lawyers enter into engagement agreements with their respective clients, and both spouses and both lawyers enter into a stipulation that they will conduct the divorce under the principles of collaborative divorce. Each lawyer agrees that the lawyer will not represent either spouse in adversarial proceedings. The lawyers and their respective clients agree to waive confidentiality and the right to object to requests for information, and agree affirmatively to provide full, honest and open disclosure of all information, whether requested or not. The lawyers agree to withdraw if their respective clients propose to withhold or misrepresent information. The lawyers also agree to not take unfair advantage of (and, in fact, to correct) each other’s mistakes. This process has been discussed in three separate articles in the May 2002 issue of Wisconsin Lawyer.<sup>40</sup> One of the authors makes a compelling case that the ethical and malpractice issues inherent in the collaborative divorce model are insurmountable. He bases his opinion on the argument that the stipulation entered into by all of the parties and lawyers causes each lawyer to “represent” both spouses, not just the spouse who nominally retained the lawyer. Whether his argument will prove persuasive remains to be seen, but even to proponents of collaborative divorce, his viewpoint should serve as a warning as well as a road map to the careful structuring of such a representation.<sup>41</sup>

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<sup>40</sup> The articles are collected at the Wisconsin State Bar web site. The link at time of publication is <http://www.wisbar.org/wislawmag/2002/05/young.html>.

<sup>41</sup> The authors suggest that there are five potential models for handling a divorce. First, both parties may proceed pro se. Second, one party may be represented and the other may proceed pro se. Third, both parties may be independently represented. Fourth, the parties may be independently represented

Attorneys should also exercise caution with respect to joint representation in the preparation of a marital property agreement if the effect is a change in the character of an asset or assets that significantly affects the composition of the property subject to division at divorce. *See* Wis. Stat. § 767.255(2)(a). For example, a marital property agreement may reclassify an asset acquired by gift or transfer at death to marital property, which would not otherwise be subject to property division under section 767.255 except upon a finding of hardship. This may result in the reclassified asset becoming subject to property division under the rationale of *Bonnell v. Bonnell*, 117 Wis. 2d 241, 344 N.W.2d 123 (1984). Whether joint representation is appropriate in such a situation will depend on a consideration of the circumstances, including the factors discussed at section 14.5, *supra*. *See also supra* § 14.11.

## **V. [§ 14.35] Sample Letter Regarding Marital Property Agreement Representation**

This sample letter relates to representing spouses in the preparation of a general marital property agreement, as discussed at section 14.27, *supra*. It should be tailored for the facts involved, and it should not be used without consideration of the ethical requirements and factors discussed in this chapter.

Dear [Both Parties]:

You have asked us to perform professional services in connection with the preparation of a Marital Property Agreement.

Before proceeding, it is imperative that each of you understands that this “joint representation” involves differing interests, as well as potential or actual conflicts of interest. These affect our ability to serve each of you with independent professional advice. In addition, adherence to the lawyer’s duty to preserve each client’s confidences may not be possible.

On the other hand, in amicable circumstances such as these, where each of you apparently has the same overall objectives, the use of one attorney or firm can assist in developing the Agreement, encourage the resolution of possible differing interests, and, of course, produce cost savings and efficiencies.

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by lawyers in a collaborative divorce. Fifth, the parties may retain a single lawyer as a mediator. The last two alternatives in particular require special attention to ethical requirements.

In serving you jointly, we will strive not to be an advocate for either of you. However, this may not be possible, and it may result in favoring one of you to the detriment of the other. Similarly, we cannot keep information confidential between the two of you, since we will be serving both of you. Therefore, by requesting this joint representation, each of you is authorizing us to reveal all information relating to each party's income, assets and liabilities, contents of documents, and other disclosures and information, to the other party.

Our recommendations concerning the Agreement will affect each of your interests in assets and income during your marriage, in the event of a divorce, and at the time of the death of one or both of you. [The present and future classification of assets and income under the Wisconsin Marital Property Act is of major significance. There may be substantial differences in resolving which assets are now or should become marital, individual, or other types of property, and the extent of your present or future respective interests in these assets and income and in mixed property.] [The classification of present and future assets and income under the Wisconsin Marital Property Act is of major significance. There may be substantial differences in resolving whether, or to what extent, your future acquired assets or income should become marital, individual, or other types of property, and the extent of each of your future respective interests in these assets and income and in mixed property.] *[Use first bracketed language for an agreement between spouses and second bracketed language for a premarital agreement.]*

Similarly, the Agreement will affect your respective rights over the management of assets, ability to obtain credit, responsibilities to creditors, duty of support, decision making during marriage, and related subjects. Also, our recommendations will affect the income, property, and other obligations of either of you in the event of termination of your marriage or in the event of your death.

There are other areas of differing interests or potential conflicts, such as the incidence of gift, income, or estate taxation, various consents to contemplated actions, duties of good faith with respect to managing marital property, and myriad other possible differing interests.

In this matter, or in any other matter, each of you may prefer to have, and should feel free to seek, the advice of separate counsel so that each of your interests will be fully protected, your confidences will not be compromised, and each of you will have the benefit of completely independent advice. Indeed, as to the question itself of whether you both should proceed with joint representation, either of you should feel entirely free to seek, and are encouraged to obtain, the advice of another attorney.



Each of you should decide whether you wish our firm to represent you jointly in connection with the development of your Marital Property Agreement, its preparation, and these related matters. Assuming that you wish to consent to our proceeding on behalf of both of you on such a joint representation basis, please sign and return the enclosed copy of this letter. Please contact me if you have any questions concerning any of this explanation.

Very truly yours,

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Each of us have reviewed the above, and we each realize that there are many areas of differing interests, as well as potential or real conflicts of interest, between us in connection with a proposed Marital Property Agreement for us and related matters. We each understand that, at any time, either of us may have separate, independent counsel in connection with these matters. After considering all of the above, we each request that you and your firm represent both of us in connection with the development of our Marital Property Agreement, its preparation, and related matters, and we each consent to that joint representation. We each also understand that, as between each of us and you and your firm, there are no confidential communications since you represent both of us (but that, with respect to third persons, the ethical rules relating to confidential communications will continue to apply).

---

[Wife] [Prospective Wife]

---

[Husband] [Prospective Husband]

## **VI. [§ 14.36] Sample Letter Regarding Estate Planning Representation**

This sample letter relates to representing spouses in the preparation of an estate plan, as discussed in section 14.32, *supra*. It should be tailored for the facts involved, and it should not be used without consideration of the ethical requirements and factors discussed in this chapter.

Dear [Wife and Husband]:

You have asked us to perform various estate planning services for you.

Before proceeding, it is important that each of you understands that this “joint representation” involves differing interests, if not potential or actual conflicts of interest. These may affect our ability to serve each of you with independent professional advice. In addition, adherence to the lawyer’s duty to preserve each client’s confidences may not be possible.

On the other hand, in amicable circumstances such as these, where each of you apparently has the same overall objectives, the use of one attorney or firm can assist in developing a coordinated overall plan, encourage the resolution of possible differing interests, and, of course, produce cost savings and efficiencies.

In serving you jointly, we will strive not to be an advocate for either of you. However, this may not be possible, and it may result in favoring one of you to the detriment of the other. Similarly, we cannot keep information confidential between the two of you, since we will be serving both of you. Therefore, by requesting this joint representation, each of you is authorizing us to reveal each party’s income, assets and liabilities, contents of documents, and other disclosures and information, to the other party.

Our recommendations concerning your estate planning will affect each of your interests in assets and income, both during your lifetimes and after your deaths. The classification of property under the Wisconsin Marital Property Act is of major significance. There may be substantial differences in resolving which assets are marital, individual, or other types of property, and the extent of your respective interests in these assets and in mixed property. Our recommendations, and your actions, will naturally affect the income, property, and other obligations of either of you in the event of termination of your marriage or at the death of one or both of you.

Similarly, your desires may differ with respect to how you wish your property to pass upon each of your deaths, or by gifts. There are other areas of differing interests or potential conflicts, such as the incidence of gift, income, or estate taxation, various consents to contemplated actions, management and control rights that you have with respect to your marital property, duties of good faith with respect to managing marital property, and myriad other possible differing interests.

In all the various aspects of your planning, or in any other matter, each of you may prefer to have, and should feel free to seek, the advice of separate counsel so that each of your interests will be fully protected, your confidences will not be compromised, and each of you will have the benefit of completely independent advice. Indeed, as to the question itself of whether you should proceed with joint representation, either of you should feel entirely free to seek, and are encouraged to obtain, the advice of another attorney.

Each of you should decide whether you wish our firm to represent you jointly in connection with your estate planning and these related matters.

Assuming that you wish to consent to our proceeding on behalf of both of you on such a joint representation basis, please sign and return the enclosed copy of this letter. Please contact me if you have any questions concerning any of this explanation.

Very truly yours,

---

We each have reviewed the above, and we each realize that there are many areas of differing interests, as well as potential or real conflicts of interest, between us in connection with our estate planning and related matters. We each understand that, at any time, either of us may have separate, independent counsel in connection with these matters. After considering all of the above, we each request that you and your firm represent both of us in our estate planning and related matters, and we each consent to that joint representation. We each also understand that, as between each of us and you and your firm, there are no confidential communications since you represent both of us (but that, with respect to third persons, the ethical rules relating to confidential communications will continue to apply).

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[Wife]

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[Husband]



## Ethical Considerations

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Book sections supplemented: 14.3, 14.4, 14.5, 14.7, 14.9, 14.10, 14.11, 14.12, 14.13, 14.27, 14.32, and 14.34

### 14.3 [General Approach to Representing One or Both Spouses] General Considerations

*Page 3: Amend last sentence in footnote 1*

Unless otherwise indicated, all references in this chapter to the Wisconsin Statutes are to the 2005–06 Wisconsin Statutes, as affected by acts through 2007 Wisconsin Act 19.

*Page 4: Insert new paragraphs after first partial paragraph*

On January 5, 2007, the Wisconsin Supreme Court issued an order formally adopting the new “Ethics 2000” changes to the Rules of Professional Conduct for Attorneys, effective on July 1, 2007. Wis. Sup. Ct. Order 04-07, 2007 WI 4, 293 Wis. 2d xv, *available at* <http://www.wicourts.gov/sc/rulhear/DisplayDocument.html?content=pdf&seqNo=27737>. The new rules are found in SCR chapter 20 and completely replace the prior version of that chapter.

The Wisconsin Ethics 2000 Committee, with its petition to the supreme court to revise the ethics rules, submitted comments that the court designated as “Wisconsin Committee Comments” in its final order repealing and recreating SCR chapter 20. Generally, Wisconsin Committee Comments indicate points of difference between an American Bar Association (ABA) Ethics 2000 Model Rule of Professional Conduct (hereinafter “model rule”) and the corresponding rule adopted in Wisconsin. The court also added comments where it adopted changes that differed from the model rule or deemed additional

guidance appropriate; the court designated these in its order as “Wisconsin Comments.” The court did not adopt the Wisconsin Committee Comments or the Wisconsin Comments, nor did it adopt the Preamble or ABA comments to the model rules, but these items may be consulted for guidance in interpreting and applying the new rules. *See* Wis. Sup. Ct. Order 04-07, 2007 WI 4, 293 Wis. 2d xv. The Wisconsin Committee Comments and the Wisconsin Comments, the Preamble and Scope section to the model rules, and the ABA comments have been published in the court’s final order and are reprinted as part of SCR chapter 20 in the Wisconsin Statutes.

*See also* Timothy J. Pierce & Dean R. Dietrich, *Wisconsin’s New Rules of Professional Conduct for Attorneys*, Wis. Law., Feb. 2007, at 12, available at [http://www.wisbar.org/AM/Template.cfm?Section=Search\\_Archive1&template=/cm/htmldisplay.cfm&contentid=63193](http://www.wisbar.org/AM/Template.cfm?Section=Search_Archive1&template=/cm/htmldisplay.cfm&contentid=63193); Dean R. Deitrich & Timothy J. Pierce, *Overview: Court’s Proposed Changes to Attorney Conduct Rules*, Wis. Law., July 2006, at 28, available at [http://www.wisbar.org/AM/Template.cfm?Section=Search\\_Archive1&template=/CM/HTMLDisplay.cfm&ContentID=62700](http://www.wisbar.org/AM/Template.cfm?Section=Search_Archive1&template=/CM/HTMLDisplay.cfm&ContentID=62700).

#### **14.4 [General Approach to Representing One or Both Spouses] Independent, Joint and Separate Representation**

*Pages 6–7: Amend last textual sentence in carry-over paragraph*

The new Supreme Court Rule ~~20:2.2~~ 20:1.7 continues to recognizes the propriety of a lawyer serving as an “intermediary” when the lawyer believes that the matter can be resolved on terms compatible with the clients’ best interests and that each client can make adequately informed decisions, and when each client provides informed consent to the common representation. *See infra* § 14.11.

*Page 7: Insert new paragraph after first full paragraph*

To coincide with the ABA’s Ethics 2000 revision of the model rules, ACTEC in March 2006 published its fourth edition to the *Commentaries*. The new edition may be ordered from ACTEC using the form located on the ACTEC Web site, at <http://www.actec.org/public/commorder.asp> (last visited Aug. 15, 2007). Individuals without Internet access may contact ACTEC by phone at (310) 398-1888.

**14.5 [General Approach to Representing One or Both Spouses]  
Suggested Factors for Determining Independent or Joint  
Representation**

*Page 9: Read in conjunction with third sentence in first paragraph of section*

The Ethics 2000 revisions to SCR chapter 20, *see* Supp. § 4.3, removed SCR 20:2.2 from the Rules of Professional Conduct for Attorneys as of July 1, 2007. The issues it addressed are now included in SCR 20:1.7.

*Page 11: Amend first sentence in last partial paragraph on page*

~~Further, consistent with SCR 20:2.2, the~~ The attorney should strive to accommodate differing interests, promote harmony, and avoid unnecessary discord.

**14.7 [Ethical Principles Applicable in the Marital Property  
Context] Identification of Relevant Sections of Rules of  
Professional Conduct for Attorneys and Related Authority**

*Pages 14–15: Read in conjunction with section*

On January 5, 2007, the Wisconsin Supreme Court issued an order formally adopting the new “Ethics 2000” changes to the Rules of Professional Conduct for Attorneys, effective on July 1, 2007. Wis. Sup. Ct. Order 04-07, 2007 WI 4, 293 Wis. 2d xv. The new rules are found in SCR chapter 20 and completely replace the prior version of that chapter.

The text of the new rules and related Comments are provided in Supplement sections 14.9, 14.11, 14.12, 14.13, and 14.32.

*Page 15: Delete last paragraph of section*

**14.9 [Ethical Principles Applicable in the Marital Property  
Context] [Conflict of Interest] Various Sources of Guidance**

*Pages 15–21: Read in conjunction with section*

On January 5, 2007, the Wisconsin Supreme Court issued an order formally adopting the new “Ethics 2000” changes to the Rules of

Professional Conduct for Attorneys, effective on July 1, 2007. Wis. Sup. Ct. Order 04-07, 2007 WI 4, 293 Wis. 2d xv.

The starting point for any analysis of conflicts of interest is SCR 20:1.7. The version of the new SCR 20:1.7 set out below was adopted with one significant modification from the model rule. As with the model rule, the new rule as adopted in Wisconsin requires that any informed consent be confirmed in writing; the Wisconsin rule further requires that the writing be “signed by the client.” Here is the text of the new SCR 20:1.7:

SCR 20:1.7 Conflicts of interest current clients. (a) Except as provided in par. (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

(1) the representation of one client will be directly adverse to another client; or

(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer’s responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(b) Notwithstanding the existence of a concurrent conflict of interest under par. (a), a lawyer may represent a client if:

(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;

(2) the representation is not prohibited by law;

(3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and

(4) each affected client gives informed consent, confirmed in a writing signed by the client.

The ABA comments to the model rules were not adopted by the court, but have been published and may be consulted for guidance in interpreting and applying Wisconsin’s new rules. The following are relevant portions of the ABA comments on model rule 1.7:

**Special Considerations in Common Representation**

[29] In considering whether to represent multiple clients in the same matter, a lawyer should be mindful that if the common representation fails because the potentially adverse interests cannot be reconciled, the result can be additional cost, embarrassment and recrimination. Ordinarily, the lawyer will be forced to withdraw from representing all of the clients if the common representation fails. In some situations, the risk of failure is so great that multiple representation is plainly impossible. For example, a lawyer cannot undertake common representation of clients where contentious litigation or negotiations between them are imminent or contemplated. Moreover,



because the lawyer is required to be impartial between commonly represented clients, representation of multiple clients is improper when it is unlikely that impartiality can be maintained. Generally, if the relationship between the parties has already assumed antagonism, the possibility that the clients' interests can be adequately served by common representation is not very good. Other relevant factors are whether the lawyer subsequently will represent both parties on a continuing basis and whether the situation involves creating or terminating a relationship between the parties.

[30] A particularly important factor in determining the appropriateness of common representation is the effect on client-lawyer confidentiality and the attorney-client privilege. With regard to the attorney-client privilege, the prevailing Rule is that, as between commonly represented clients, the privilege does not attach. Hence, it must be assumed that if litigation eventuates between the clients, the privilege will not protect any such communications, and the clients should be so advised.

[31] As to the duty of confidentiality, continued common representation will almost certainly be inadequate if one client asks the lawyer not to disclose to the other client information relevant to the common representation. This is so because the lawyer has an equal duty of loyalty to each client, and each client has the right to be informed of anything bearing on the representation that might affect that client's interests and the right to expect that the lawyer will use that information to that client's benefit. See Rule 1.4. The lawyer should, at the outset of the common representation and as part of the process of obtaining each client's informed consent, advise each client that information will be shared and that the lawyer will have to withdraw if one client decides that some matter material to the representation should be kept from the other. In limited circumstances, it may be appropriate for the lawyer to proceed with the representation when the clients have agreed, after being properly informed, that the lawyer will keep certain information confidential. For example, the lawyer may reasonably conclude that failure to disclose one client's trade secrets to another client will not adversely affect representation involving a joint venture between the clients and agree to keep that information confidential with the informed consent of both clients.

[32] When seeking to establish or adjust a relationship between clients, the lawyer should make clear that the lawyer's role is not that of partisanship normally expected in other circumstances and, thus, that the clients may be required to assume greater responsibility for decisions than when each client is separately represented. Any limitations on the scope of the representation made necessary as a result of the common representation should be fully explained to the clients at the outset of the representation. See Rule 1.2(c).

[33] Subject to the above limitations, each client in the common representation has the right to loyal and diligent representation and the protection of Rule 1.9 concerning the obligations to a former client. The client also has the right to discharge the lawyer as stated in Rule 1.16.

The new SCR 20:1.7 sets out a new standard for consent to a concurrent conflict of interest—namely, “informed consent.” *See* Supp. § 14.11, *infra*.

#### **14.10 [Ethical Principles Applicable in the Marital Property Context] [Conflict of Interest] Suggested Analytical Framework for Conflicts of Interest**

*Pages 21–26: Replace section*

On January 5, 2007, the Wisconsin Supreme Court issued an order formally adopting the new “Ethics 2000” changes to the Rules of Professional Conduct for Attorneys, effective on July 1, 2007. Wis. Sup. Ct. Order 04-07, 2007 WI 4, 293 Wis. 2d xv. The revised SCR chapter 20 no longer includes SCR 20:2.2. That former rule on intermediaries has been omitted from the rules as of July 1, 2007. For the text of the new SCR 20:1.7 and relevant ABA comments, see Supplement section 14.9.

#### **14.11 [Ethical Principles Applicable in the Marital Property Context] [Conflict of Interest] Consent to Joint Representation**

*Pages 26–27: Read in conjunction with footnote 26 and third paragraph of section*

On January 5, 2007, the Wisconsin Supreme Court issued an order formally adopting the new “Ethics 2000” changes to the Rules of Professional Conduct for Attorneys, effective on July 1, 2007. Wis. Sup. Ct. Order 04-07, 2007 WI 4, 293 Wis. 2d xv.

The new SCR 20:1.0 (Terminology) provides the definition of “informed consent” in subsection (f):

(f) “Informed consent” denotes the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct.

The ABA comment to this definition (numbered as rule 1.0(e) in the model rules) provides:

[6] Many of the Rules of Professional Conduct require the lawyer to obtain the informed consent of a client or other person (e.g., a former client or, under certain circumstances, a prospective client) before accepting or continuing representation or pursuing a course of conduct. See, e.g., Rules 1.2(c), 1.6(a) and 1.7(b). The communication necessary to obtain such consent will vary according to the Rule involved and the circumstances giving rise to the need to obtain informed consent. The lawyer must make reasonable efforts to ensure that the client or other person possesses information reasonably adequate to make an informed decision. Ordinarily, this will require communication that includes a disclosure of the facts and circumstances giving rise to the situation, any explanation reasonably necessary to inform the client or other person of the material advantages and disadvantages of the proposed course of conduct and a discussion of the client's or other person's options and alternatives. In some circumstances it may be appropriate for a lawyer to advise a client or other person to seek the advice of other counsel. A lawyer need not inform a client or other person of facts or implications already known to the client or other person; nevertheless, a lawyer who does not personally inform the client or other person assumes the risk that the client or other person is inadequately informed and the consent is invalid. In determining whether the information and explanation provided are reasonably adequate, relevant factors include whether the client or other person is experienced in legal matters generally and in making decisions of the type involved, and whether the client or other person is independently represented by other counsel in giving the consent. Normally, such persons need less information and explanation than others, and generally a client or other person who is independently represented by other counsel in giving the consent should be assumed to have given informed consent.

[7] Obtaining informed consent will usually require an affirmative response by the client or other person. In general, a lawyer may not assume consent from a client's or other person's silence. Consent may be inferred, however, from the conduct of a client or other person who has reasonably adequate information about the matter. A number of Rules require that a person's consent be confirmed in writing. See Rules 1.7(b) and 1.9(a). For a definition of "writing" and "confirmed in writing," see paragraphs (n) and (b). Other Rules require that a client's consent be obtained in a writing signed by the client. See, e.g., Rules 1.8(a) and (g). For a definition of "signed" see paragraph (n) [in Wisconsin, see SCR 1.0(q)].

For the text of the revised SCR 20:1.7, see Supplement section 14.9.

**14.12 [Ethical Principles Applicable in the Marital Property Context] [Conflict of Interest] Representing One Spouse Following Joint Representation**

*Page 31: Add to end of section*

On January 5, 2007, the Wisconsin Supreme Court issued an order formally adopting the new “Ethics 2000” changes to the Rules of Professional Conduct for Attorneys, effective on July 1, 2007. Wis. Sup. Ct. Order 04-07, 2007 WI 4, 293 Wis. 2d xv; *see also* Wis. Sup. Ct. Order 06-04, 2007 WI 48, \_\_\_ Wis. 2d \_\_\_ (eff. July 1, 2007), *available at* <http://www.wicourts.gov/sc/rulhear/DisplayDocument.pdf?content=pdf&seqNo=28907> (making nonsubstantive stylistic amendment to SCR 1.9(b)(2)).

The new SCR 20:1.9 has been modified to deal more flexibly with imputed conflicts that arise when lawyers change law firms. The text of the new rule follows:

SCR 20:1.9 Duties to former clients. (a) A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person’s interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in a writing signed by the client.

(b) A lawyer shall not knowingly represent a person in the same or a substantially related matter in which a firm with which the lawyer formerly was associated had previously represented a client:

(1) whose interests are materially adverse to that person; and

(2) about whom the lawyer had acquired information protected by sub.

(c) and SCR 20:1.6 that is material to the matter; unless the former client gives informed consent, confirmed in a writing signed by the client.

(c) A lawyer who has formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter:

(1) use information relating to the representation to the disadvantage of the former client except as these rules would permit or require with respect to a client, or when the information has become generally known; or

(2) reveal information relating to the representation except as these rules would permit or require with respect to a client.

### **14.13 [Ethical Principles Applicable in the Marital Property Context] Client Confidences**

*Pages 31–34: Read in conjunction with section*

On January 5, 2007, the Wisconsin Supreme Court issued an order formally adopting the new “Ethics 2000” changes to the Rules of Professional Conduct for Attorneys, effective on July 1, 2007. Wis. Sup. Ct. Order 04-07, 2007 WI 4, 293 Wis. 2d xv.

The new SCR 20:1.6 has been modified in a manner that does not materially affect the analysis in Book section 14.13. The revised rule provides as follows:

SCR 20:1.6 Confidentiality. (a) A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, except for disclosures that are impliedly authorized in order to carry out the representation, and except as stated in pars. (b) and (c).

(b) A lawyer shall reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary to prevent the client from committing a criminal or fraudulent act that the lawyer reasonably believes likely to result in death or substantial bodily harm or in substantial injury to the financial interest or property of another.

(c) A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:

(1) to prevent reasonably likely death or substantial bodily harm;

(2) to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client’s commission of a crime or fraud in furtherance of which the client has used the lawyer’s services;

(3) to secure legal advice about the lawyer’s conduct under these rules;

(4) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer’s representation of the client; or

(5) to comply with other law or a court order.

*Page 32: Amend citation after first sentence in first full paragraph on page*

SCR 20:1.8(b), 9(c)(1).

#### **14.27 [Application of Rules and Suggested Factors to Specific Joint Representation Situations] General Marital Property Agreements**

*Page 46: Amend third sentence in last paragraph*

See section 7.14, *supra*, regarding the enforceability of marital property agreements, and section ~~7.14(a)(4)~~ 7.45, *supra*, regarding the effect of lack of separate counsel.

#### **14.32 [Application of Rules and Suggested Factors to Specific Joint Representation Situations] Estate Planning**

*Page 56: Replace second sentence in first full paragraph on page and accompanying quotation*

The rule for this situation is found in SCR 20:1.8, which, as of July 1, 2007, provides:

A lawyer shall not solicit any substantial gift from a client, including a testamentary gift, nor prepare an instrument giving the lawyer or a person related to the lawyer any substantial gift from a client, including a testamentary gift, except where (1) the client is related to the donee, (2) the donee is a natural object of the bounty of the client, (3) there is no reasonable ground to anticipate a contest, or a claim of undue influence or for the public to lose confidence in the integrity of the bar, and (4) the amount of the gift or bequest is reasonable and natural under the circumstances. For purposes of this paragraph, related persons include a spouse, child, grandchild, parent, grandparent or other relative or individual with whom the lawyer or the client maintains a close, familial relationship.

#### **14.34 [Application of Rules and Suggested Factors to Specific Joint Representation Situations] Divorce**

*Pages 60–63: Read in conjunction with section*

Note that the references to section 767.255 and subsections of that statute in Book section 14.34 should be modified to refer to section 767.61 and the corresponding subsections of that statute. Similarly, the reference to section 767.26(8) in Book section 14.34 should be modified to refer to section 767.56(8). No substantive change has occurred with respect to these provisions, being part of a reorganization of chapter 767 effected by 2005 Wisconsin Act 443.

*Page 61: Read in conjunction with last sentence in first full paragraph on page and footnote 39*

The Ethics 2000 revisions to SCR chapter 20, *see* Supp. § 4.3, removed SCR 20:2.2 from the Rules of Professional Conduct for Attorneys as of July 1, 2007. The concepts covered in that rule are now addressed in SCR 20:1.7.

*Page 61: Amend last partial sentence on page*

Section ~~767.255(3)(L)~~ 767.61(3)(L) provides that a written agreement by spouses or parties intending to be married “concerning any arrangement for property distribution” is a factor to be considered by the court in . . . .

*Page 62: Amend second full sentence on page*

In addition, section ~~767.26(8)~~ 767.56(8) provides that agreement concerning financial support is a factor to be considered by the court in determining maintenance payments.

*Page 63: Amend first citation and second textual sentence in first paragraph on page*

*See* Wis. Stat. § ~~767.255(2)(a)~~ 767.61(2)(a). For example, a marital property agreement may reclassify an asset acquired by gift or transfer at death to marital property, which would not otherwise be subject to property division under section ~~767.255~~ 767.61 except upon a finding of hardship.





# Appendices

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# **Appendix A**

## **The Uniform Marital Property Act with Comments**

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**UNIFORM MARITAL PROPERTY ACT  
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### Uniform Marital Property Act Prefatory Note

"The institution of property is the embodiment of accidents, events, and the wisdom of the past. It is before us as clay into which we can introduce the coloration and configuration representing our wisdom. How great, how useful this new ingredient may be will largely determine the future happiness, and perhaps the continued existence of our society."

Powell, *The Law of Real Property* (Rohan 4th ed. 1977).

Marriages have beginnings and endings. For their participants, the period between these points is the marriage. This Act is a property law. It functions to recognize the respective contributions made by men and women during a marriage. It discharges that function by raising those contributions to the level of defined, shared and enforceable property rights at the time the contributions are made.

The challenge to create such a framework is not new. Basic differences in approaches to marital economics go back for many centuries. See Donahue, *What Causes Fundamental Legal Ideas? Marital Property in England and France in the Thirteenth Century*, 78 Mich. L. Rev. 59 (1979); Younger, *Marital Regimes: A Story of Compromise and Demoralization, Together with Criticism and Suggestions for Reform*, 67 Cornell L. Rev. 45 (1981). In modern times the challenge was well articulated twenty years ago by the Report of the Committee on Civil and Political Rights to the President's Commission on the Status of Women. In 1963 that Report said:

Marriage is a partnership to which each spouse makes a different but equally important contribution. This fact has become increasingly recognized in the realities of American family living. While the laws of other countries have reflected this trend, family laws in the United States have lagged behind. Accordingly, the Committee concludes that during marriage each spouse should have a legally defined and substantial right in the earnings of the other spouse and in the real and personal property acquired as a result of such earnings, as well as in the management of such earnings and property. Such right should survive the marriage and be legally recognized in the event of its termination by annulment, divorce, or death. This policy should be appropriately implemented by legislation which would safeguard either spouse against improper alienation of property by the other.

In the twenty years after those words much has changed regarding the institution of marriage, even though the challenge has not been fully met.

A prime example is the very demography of marriage and its terminal events. In 1963, 66.31% of all terminated marriages ended by death and 33.69% by divorce. By 1979 only 42.77% terminated by death, while 57.23% ended by dissolution. For half a decade the ratio of marriages to dissolution has been about two to one. The latest figures were 2,438,000 marriages and 1,219,000 divorces in 1981. The two to one ratio contrasts with 1930, when there were six marriages to every dissolution.

Statistics are not the only evidence of dramatic change. Statehouses have reflected it. Beginning with California at the end of the 60's and promulgation of the Uniform Marriage and Divorce Act in the early 70's, no-fault divorce has swept the statute books. In 1983 Illinois and South Dakota stand alone in adhering to fault-based divorce, and efforts to change to no-fault continue in Illinois. "Equitable distribution" of property became the handmaiden of no-fault divorce in the Uniform Marriage and Divorce Act and in most other reforms. Forty-one traditional common law jurisdictions now use some form of *property division* as a principal means of resolving economic dilemmas on dissolution. Adding the eight community property jurisdictions in which such a division is an inherent aspect of spousal property rights yields a total of 49. The one state missing on the property division roster is Mississippi. These property division developments address and typically adopt sharing concepts and bring many common law jurisdictions close to a deferred community property approach to divorce. Cheadle, *The Development of Sharing Principles in Common Law Marital Property States*, 28 UCLA L. Rev. 1269 (1982); see also Younger, *op. cit., supra*.

The ferment of change has not been limited to dissolution. The Uniform Probate Code was promulgated in 1969. Fourteen states are now listed as Code states or as substantially conforming states. Article II of the Code contains the concept of an augmented estate. It borrows heavily from New York's 1966 version of the idea. It is an advance on traditional forced-share procedures, operating by the creation of a larger universe of property against which a spousal right of election is exercisable. It accomplishes this by penetrating the veil of title and other techniques which have developed to insulate assets from the reach of forced-share statutes. In the official comment to the Code the augmented estate provisions are described as preventing arrangements by the owner of wealth which would transmit property to other than a surviving spouse by means other than probate for the deliberate purpose of defeating the rights of a surviving spouse.

It is worth noting that the Code's provisions, as well as conventional forced-share provisions in common law states, leave a gap. They transform assets into a sharing mode in a meaningful way only when the "have-not" spouse survives. If the sequence of death is the opposite, the have-not spouse has no power to dispose of assets over which he or she has no title in any common law jurisdiction.

The long-arm augmented estate provisions of the Uniform Probate Code may not go far enough to accommodate the perception of most laymen. A significant empirical study published in 1978 indicates a widespread public preference for a distribution of an *entire* intestate estate to a surviving spouse, whether or not there are surviving children. Fellows, Simon & Rau, *Public Attitudes About Distribution At Death And Intestate Succession Laws In The United States*, 1978 Am. B. Found. Research J. 319.

Obviously the "everything to each other" mode is confined to dispositions at death. An imposing body of case law testifies to a paradigm shift in this view when the question of "Who should get what and when?" is asked at a dissolution! And it is the equitable distribution court's demanding role in the judicial process to monitor and referee the ensuing contests in the divorce courts. Burgeoning advance sheets clearly indicate just how difficult the referee's job is when it must be done well over a million times a year!

In 1981 yet another shift was added to the catalog of change. After years of debate, tax-free interspousal transfers entered the stage under the auspices of the Economic Recovery Tax Act of 1981. *Wall Street Journal* columnist Vermont Royster furnished a characteristically succinct summary of it all:

"The marriage ceremony may say you two are now one and even include that phrase about with all my worldly goods I thee endow. The Internal Revenue Service has always taken a different view. It's wanted its share. .... wait until January 1, 1982, and .... after that magic date you can share with your spouse as much as you please of those worldly goods .... without so much as a by-your-leave from the federal tax man. In 1982 no more gift and estate taxes between spouses." *Wall St. J.*, Sept. 2, 1981.

Heavy economic responsibilities of married couples and methods of coping with them point to yet another trendline of the last few decades. It is that of the two-worker households in which sharing the burden of producing family income is becoming routine. In more than half of American marriages with two spouses present there is a working wife and the number is growing. When there are children, the ratio is even higher. In more than two-thirds of current upper income marriages (\$24,000 or more) there are two wage earners. Sharing of responsibility for wages from *outside* the home is altering traditional spousal roles and particularly economic roles, rights, and responsibilities.

Thus the stage is set by substantial social and legislative change in the duration of marriages and in the economics of the termination of marriages by dissolution and death.

The Uniform Marital Property Act makes its appearance on that stage to offer a means of establishing present shared property rights of spouses *during* the marriage. This approach is bottomed on two propositions. The first is creation of an immediate sharing mode of ownership. The second proposition is that the sharing mode during marriage is an ownership right already in existence at the end of a marriage. Thus recognition and perfection of shared and vested ownership rights in marital property are in place at divorce or death. They do not have to come to fruition as a result of a court-ordained and possibly adversary "division" or by a statutorily-sanctioned "transfer."

Is the Uniform Marital Property Act a panacea for the malaise of marriage? Will it lower the divorce rate? Save the family? Eliminate marital violence? Be fully comprehensible? Be welcomed by all? Lower the cost of the family house? Create better parents? Solve child abuse? Avoid probate? Lower the cost of death or divorce?

Perhaps some but certainly not all of the above. If it does affect any of those considerations, it will take time and the process will be subtle. The disintegrating forces operating on marriages and families are many and complex. It would be a bold claim to suggest that any legislation could fully identify and rectify the problems in such an area. But the obvious and apparent existence of problems in the economic area of marriage certainly justifies an effort to identify and rectify them. The Uniform Marital Property Act is precisely such an effort.

What are the root concepts?

FIRST: Property acquired during marriage by the effort of spouses is shared and is something the couple can truly style as "ours." Rather than an evanescent hope, the idea of sharing implicit in viewing property as "ours" becomes reality as a result of a present, vested ownership right which each spouse has in all property acquired by the personal efforts of either during the marriage. That property is "marital property." (Section 4).

Except for its income, property brought into the marriage or acquired afterward by gift or devise is not marital but "individual property." Its *appreciation* remains individual property. However, the *income* of that property becomes marital property, so that *all* income of a couple is marital property. (Section 4).



Property already owned when the Act becomes effective or owned by couples moving into an adopting state will take on the characteristics of marital property only at death or marital dissolution and then only if it would have been marital property under the Act had the Act been in effect when and where the property was acquired. Prior to death or dissolution the Act ordains no change in the classification of property of a couple acquired at a time when the Act did not apply. (Section 4(h), 17 and 18).

SECOND: The system which the Act creates to manage and control marital property accords a considerable measure of individual option. "Management and control" is a phrase of art in the Act. Basically management and control rights flow from the form in which title to property is held. If only one spouse holds property there is no requirement for the other spouse to participate in management and control functions. If both spouses hold property they must both participate in management and control unless the holding is in an alternative ("A or B") form. Couples can select their own options as they deem appropriate. (Sections 3, 5, 10 and 11). Management and control is different from ownership. Ownership rights are not lost by relinquishing or even neglecting management and control rights. In essence, the Act's management and control system is substantially similar to the existing procedures of title based management in common law states. (Section 5).

To guard against possible abuses by a spouse with sole title, a court can implement the addition of the name of the other spouse to marital property so that it is held, managed and controlled by both spouses. (Section 15).

The rule on gifts of marital property to third parties provides a safe harbor for smaller gifts. Unless aggregate gifts of marital property by one spouse to a third party in a calendar year are less than a specified dollar amount or are reasonable in amount with respect to the economic position of the spouses when made, both spouses must join in making the gift. A failure to procure that joinder renders the gift voidable at the option of the non-participating spouse. (Section 6).

THIRD: The varying patterns of today's marriages are accommodated by an opportunity to create custom systems by "marital property agreements." Full freedom to contract with respect to virtually all property matters is possible under the Act. By a marital property agreement a couple could opt-out of the provisions of the Act in whole or in part. Conversely, they could opt-in by agreeing that the Act's provisions will apply to all or a part of the property they own before they became subject to its terms.

As a protection, and to ease matters of proof, the Act requires that marital property agreements be made in writing and signed by both spouses. (Section 10). Marital property agreements are enforceable without consideration.

FOURTH: On dissolution the structure of the Act as a *property statute* comes into full play. The Act takes the parties "to the door of the divorce court" only. It leaves to existing dissolution procedures in the several states the selection of the appropriate procedures for dividing property. On the other hand the Act has the function of confirming the *ownership* of property as the couple enters the process. Thus reallocation of property derived from the effort of both spouses during the marriage starts from a basis of the equal undivided ownership that the spouses share in their marital property. A given state's equitable distribution or other property division procedures could mean that the ownership will end that way, or that it could be substantially altered, but that will depend on other applicable state law and judicial determinations. An analogous situation obtains at death; with the Act operating primarily as a property statute rather than a probate statute.

At divorce and death special provisions will apply to property of a couple acquired before the Act applied to that couple. If any of that property would have been marital property under the Act, had the Act been in effect when and where it was acquired, then such property will be treated as if it were marital property at divorce. Property of the deceased spouse having that characteristic will be treated in that manner at death. This represents a deferred approach to reclassification of the property of spouses which does not otherwise have the characteristics of marital property due to the time or place of its acquisition. The deferral is to the time of marital termination at divorce or death. Those are events at which states have long altered the classification of their citizens' property by equitable distribution provisions or by forced share and augmented estate provisions. The Act builds on those established patterns already followed by the states by creating the deferred classification with respect to property owned by couples before the Act applied to them. A provision effecting automatic reclassification of such property with the passage of the Act would amount to retroactive legislation and would risk constitutional attack. See Irish, *A Common Law State Considers A Shift to Community Property*, 5 Community Prop. J. 227 (1978). On the other hand, the deferred approach of the Act operates only prospectively, tracking the procedure of the bulk of existing state legislation that prescribes forms of marital sharing effective only at divorce or death. (Sections 17 and 18).

FIFTH: Creditors may have claims that arise before marriage and after marriage. The premarital creditor is denied a bonanza by a marriage. (Section 8(b) (iii)). That creditor can only reach what would have been reached had there been no marriage. Postmarital obligations may subject both marital and individual property to claims. Obligations incurred by a spouse during marriage are presumed to be incurred in the interest of the marriage and the family and those obligations may be satisfied from all marital property and the other property of the incurring spouse. (Section 8(a) and (b) (ii)).

SIXTH: Bona fide purchasers of property for value are protected in their transactions with spouses by reliance on the manner in which property is held. They are under no duty to look "underneath" the manner of holding and are fully protected for not doing so. (Section 9).

In addition to those root concepts, a series of enabling provisions offer convenient support for the system. These include special methods of holding property, including a survivorship form of ownership (Section 11); dispositions by a probate avoidance feature in marital property agreements (Section 10(c)(6)); and remedies for disputes between the spouses affecting their property, including interspousal property accountings (Section 15). There are procedures to deal with marital and individual property which becomes intermixed. (Section 14). Special rules deal with complex property rights in life insurance and deferred employee benefits. (Sections 12 and 13). Conventional concurrent and survivorship forms may be used for marital property. (Section 11(d)). As an option for use in states that recognize tenancy by the entireties, existing tenancy by the entireties property continues to be available to perpetuate the creditor protection it affords. (Section 19).

Some of the root concepts can be traced to the sharing ideal which is at the center of the historical community property approach. The fundamental principle that ownership of all of the economic rewards from the personal effort of each spouse during marriage is shared by the spouses in vested, present, and equal interests is the heart of the community property system. It is also the heart of the Uniform Marital Property Act. Common law states have been moving closer and closer to the sharing concept in both divorce and probate legislation, and the Uniform Marital Property Act builds on the direction of that movement. Sharing is seen as a system of elemental fairness and justice so that those who share in the many and diverse forms of work involved in establishing and maintaining a marriage will have a protected share in the material acquisitions of that marriage. The Act creates and protects that share without forcing a spouse to await the completion of a gift from the other spouse or the garnering of proof of dollar-for-dollar contributions to the purchase price of assets acquired over the years of marriage. Under the Act, the sharing of property is recognized by creation of a present interest simultaneously with acquisition of property by effort during marriage. The interest is legally defined and enforceable. It permeates assets as they are acquired and continues to permeate them as they are invested and reinvested, as they are exchanged and transferred, and as they grow or diminish.

Such a law translates the emotional and perceived concept of "ours" into a verified legal reality. And while that parallels sharing under community property systems, the Act is more accurately characterized as a *sui generis* approach, and as one which utilizes equally useful ideas developed in common law jurisdictions, such as title based management and control. In addition, it is a response to the twenty-year-long challenge of the President's Commission on the Status of Women issued in 1963 to face the reality that each spouse makes a different but equally important contribution in a marriage. Though drafted with an awareness of various community property statutes and cases, the Uniform Marital Property Act is not an image of any of them. It is a statute speaking to the realities and equities of marriages in America in the Eighties.

## UNIFORM MARITAL PROPERTY ACT

## SECTION 1. GENERAL DEFINITIONS.

In this [Act]:

- (1) "Acquire" in relation to property includes reduction of indebtedness on encumbered property and obtaining a lien on or security interest in property.
- (2) "Appreciation" means a realized or unrealized increase in the value of property.
- (3) "Decree" means a judgment or other order of a court.
- (4) "Deferred employment benefit" means a benefit under a plan, fund, program, or other arrangement under which compensation or benefits from employment are expressly, or as a result of surrounding circumstances, deferred to a later date or the happening of a future event. Such an arrangement includes a pension, profit sharing, or stock-bonus plan; an employee stock-ownership or stock-purchase plan; a savings or thrift plan; an annuity plan; a qualified bond-purchase plan; a self-employed retirement plan; a simplified employee pension; and a deferred compensation agreement or plan. It does not include life, health, accident, or other insurance, or a plan, fund, program, or other arrangement providing benefits comparable to insurance benefits, except to the extent that benefits under the arrangement: (i) have a present value that is immediately realizable in cash at the option of the employee; (ii) constitute an unearned premium for the coverage; (iii) represent a right to compensation for loss of income during disability; or (iv) represent a right to payment of expenses incurred before time of valuation.
- (5) "Determination date" means the last to occur of the following: (i) marriage; (ii) 12:01 a.m. on the date of establishment of a marital domicile in this state; or (iii) 12:01 a.m. on the effective date of this [Act].
- (6) "Disposition at death" means transfer of property by will, intestate succession, nontestamentary transfer, or other means that take effect at the transferor's death.
- (7) "Dissolution" means: (i) termination of a marriage by a decree of dissolution, divorce, annulment, or declaration of invalidity; or (ii) entry of a decree of legal separation or separate maintenance.
- (8) "During marriage" means a period that begins at marriage and ends at dissolution or at the death of a spouse.
- (9) Property is "held" by a person only if a document of title to the property is registered, recorded, or filed in a public office in the name of the person or a writing that customarily operates as a document of title to the type of property is issued for the property in the person's name.
- (10) "Income" means wages, salaries, commissions, bonuses, gratuities, payments in kind, deferred employment benefits, proceeds, other than death benefits, of a health, accident, or disability insurance policy, or of a plan, fund, program, or other arrangement providing benefits comparable to those forms of insurance, other economic benefits having value which are attributable to the effort of a spouse, dividends, interest, income from trusts, and net rents and other net returns attributable to investment, rental, licensing, or other use of property, unless attributable to a return of capital or to appreciation.
- (11) "Management and control" means the right to buy, sell, use, transfer, exchange, abandon, lease, consume, expend, assign, create a security interest in, mortgage, encumber, dispose of, institute or defend a civil action regarding, or otherwise deal with, property as if it were property of an unmarried person.
- (12) "Marital property agreement" means an agreement that complies with Section 10.
- (13) A person has "notice" of a fact if the person has knowledge of it, receives a notification of it, or has reason to know that it exists from the facts and circumstances known to the person.
- (14) "Presumption" or a "presumed" fact means the imposition on the person against whom the presumption or presumed fact is directed of the burden of proving that the nonexistence of the presumed condition or fact is more probable than its existence.

(15) "Property" means an interest, present or future, legal or equitable, vested or contingent, in real or personal property.

(16) "Written consent" means a document signed by a person against whose interests it is sought to be enforced.

#### Comment

1. The definition of "acquiring" assures the inclusion in the word of all transactions which increase dominion and control over assets. In a typical marital situation, payment on a mortgage will be an important means of building assets. The definition makes it clear that this is a means of acquisition.

2. "Appreciation" has certain differential consequences, depending on whether it is from individual property or is created or enhanced by the effort of one spouse expended on individual property of the other spouse. The definition makes it clear that a specific realization, such as a sale, is *not* necessary for it to be a factor in marital property economics.

4. The major provisions of the definition are derived from The Employee Retirement Income Security Act of 1974 ("ERISA"), Pub. L. No. 93-406. In the Act the definition is intended to cover and include plans of both private and public employers.

5. The Act will apply to those couples now domiciled in an adopting state as well as those who move to one in the future. It will also apply to couples who marry in an adopting state after the Act is in effect. The definition of "determination date" creates a flexible formula to establish for individual couples in these three separate configurations the specific date as of which the Act is in effect with respect to their property. Use of 12:01 a.m. as the triggering incident of the determination date eliminates the necessity of referring throughout the Act to events occurring "on or after" the determination date.

7. A legal separation or decree of separate maintenance is a dissolution. Specific authority to deal with the consequences of a legal separation is included as bracketed Subsection (4) of Section 17 for states in which this procedure is still in use. It is suggested that the term should remain in the definition even if this subsection is not enacted in order to deal with possible multi-state problems that could involve a state still using the procedure.

8. The Act concerns the property of married persons. If a man and a woman are not married, the property they own is *not* marital property. It may have been marital property if their marriage has been dissolved, or if one of them is deceased, but on the occurrence of such an event it loses its classification as marital property. Consequently the term "during marriage" applies throughout the Act and describes a particular status. The period when certain property will be marital is during marriage and the Act's provisions addressed to "spouses" will apply then as well. Without marriage, a man and a woman are not spouses. When they are referred to as spouses, the connotation is that the event or relationship referred to takes place during marriage.

9. The word "title" is often viewed as the equivalent of "ownership." In the Act the method of referring to property to which there is typical and usual form of documentation of title is that of identifying it as being "held" by a person named in the documentation, since title is *not* synonymous with ownership in the Act. The concept of holding is used to avoid a continued reference to title and a construction that might encourage overlooking the separate legal status of title and ownership, which is a fundamental aspect of the Act. The result of the definition is that there will be some types of property that will not be held by either spouse. This is obviously true with respect to classic forms of bearer property without the Act, and the Act does not disturb that circumstance.

10. Section 4 classifies all income earned or accrued during marriage and after the determination date from any source as marital property. The "income" definition is a broad one and is intended to cover all forms of income and earnings, but to exclude returns of capital and appreciation.

11. Management and control issues are faced daily by partners and owners of various concurrent interests. They are solved daily as well. The management and control function is central to the Act, and the way in which the definition is applied is covered in Section 5.

14. The presumption provisions are derived from Rule 301(a) of the Uniform Rules of Evidence.

16. There are two types of writings that have special significance under the Act. One is a marital property agreement, fully described in Section 10. The other is the "written consent." This is a writing that states facts or consequences chargeable to and enforceable against a signatory. A written consent may have one or more signatories. It could be a conventional contract signed by two or more persons or it could be a simple memorandum of a type that would satisfy a statute of frauds requirement, signed by only one person. As an

example, a creditor can relinquish a right to proceed against marital property by the terms of Section 8(d). This is accomplished by a written consent, and that would be a one-signatory document affirming the relinquishment. As additional examples, Section 12(c)(5) specifies that a written consent of one spouse permits relinquishment of rights in a life insurance policy, while in Section 12(c)(6) the written consents of both spouses are prerequisites to another method of dealing with life insurance.

## SECTION 2. RESPONSIBILITY BETWEEN SPOUSES.

(a) Each spouse shall act in good faith with respect to the other spouse in matters involving marital property or other property of the other spouse. This obligation may not be varied by a marital property agreement.

(b) Management and control by a spouse of that spouse's property that is not marital property in a manner that limits, diminishes, or fails to produce income from that property does not violate subsection (a).

### Comment

Spouses are not trustees or guarantors toward each other. Neither are they simple parties to a contract endeavoring to further their individual interests. The duty is between, and is one of good faith. A spouse is not bound always to succeed in matters involving marital property ventures, but while endeavoring to succeed in a venture, must proceed with an appropriate regard for the property interests of the other spouse and without taking unfair advantage of the other spouse. See Cal. Civ. Code Sec. 5125(e) (Supp. 1980) for a similar provision in use in that state. See also Reppy, *Community Property in California*, pp. 174-75, 177 (1980). This is one of four provisions in the Act that cannot be varied by a marital property agreement. (Section 10(c)).

Subsection (b) clarifies the right of a spouse to regulate the income stream of property of that spouse that is not marital property without violating the Section. Since all income of that property during marriage and after the determination date is marital property, a question might arise regarding the application of Subsection (a) to the income stream. Subsection (b) resolves that question.

## SECTION 3. VARIATION BY MARITAL PROPERTY AGREEMENT.

Except as provided in Sections 2, 8 (e), 9 (c) and 10 (b), a marital property agreement may vary the effect of this [Act].

### Comment

This section is modeled on UCC Section 1-102(3). It is placed at this point in the chronology in the Act in order that its message be conveyed early and emphatically. The Act's property system applies if it is not changed. However, with four very limited exceptions (those of the good faith duty of Section 2, the protection of third parties under Sections 8(e) and 9(c), and the support of dependent children under Section 10(b)), there is freedom to change the Act by a marital property agreement. Thus, a couple may opt-out, opt-in, or do both in part. Custom-tailored marital property regimes are possible. The Act permits a couple to move its marital economics from status to contract and encourages a type of interspousal contractual freedom little known in common law states. It is important to the operation of the Act that the significance of this section be carried through to the use and application of its various provisions. For example, it is clearly intended that contractual variance is possible with respect to Section 4 (classification generally), Section 5 (management and control), Section 12 (life insurance classification), Section 13 (classification of employee benefits), Section 17 (marital dissolution), and Section 18 (disposition at death), although these are only examples. The provisions of this Section and Section 10 should always be read as a part of every other provision of the Act.

## SECTION 4. CLASSIFICATION OF PROPERTY OF SPOUSES.

(a) All property of spouses is marital property except that which is classified otherwise by this [Act].

(b) All property of spouses is presumed to be marital property.

(c) Each spouse has a present undivided one-half interest in marital property.

(d) Income earned or accrued by a spouse or attributable to property of a spouse during marriage and after the determination date is marital property.

(e) Marital property transferred to a trust remains marital property.

(f) Property owned by a spouse at a marriage after the determination date is individual property.

(g) Property acquired by a spouse during marriage and after the determination is individual property if acquired:

(1) by gift or a disposition at death made by a third person to the spouse and not to both spouses;

(2) in exchange for or with the proceeds of other individual property of the spouse;

(3) from appreciation of the spouse's individual property except to the extent that the appreciation is classified as marital property under Section 14;

(4) by a decree, marital property agreement, written consent, or reclassification under Section 7 (b) designating it as the individual property of the spouse;

(5) as a recovery for damage to property under Section 15, except as specifically provided otherwise in a decree, marital property agreement, or written consent; or

(6) as a recovery for personal injury except for the amount of that recovery attributable to expenses paid or otherwise satisfied from marital property.

(h) Except as provided otherwise in this [Act] the enactment of this [Act] does not alter the classification and ownership rights of property acquired before the determination date.

(i) Except as provided otherwise in this [Act] and to the extent it would affect the ownership rights of the spouse that existed in the property before the determination date, during marriage the interest of a spouse in property owned immediately before the determination date is treated as if it were individual property.

#### Comment

The Section creates the heart of the Act. It contains a general presumption, a series of property rules, an income rule, classification rules, and transition rules.

*Classification:* "Classification" is an essential process in applying the Act. In classification the essential sorting process is taking place: What is a given item or aggregation of property? Marital property? Individual property? Property owned before the determination date which had a wholly different set of ownership incidents not established by the Act at all? All property has a classification — a generic and basic set of characteristics — and the process is devoted to establishing those precise characteristics and answering those questions. The most important parts of the answer depend on *source* and *time of acquisition*. Title is *not* an answer since title functions under the Act principally to establish management and control rights and the facilitation of third party transactions flowing from the exercise of management and control rights. Under the Act title does *not* function as a classification index. Reclassification is just what the word implies — it is a change in classification, generally from marital to individual or vice versa.

*The General Presumption:* The first building block in the Act's operation is the general presumption in Subsection (b). The bias of the presumption favors classifying spousal assets as marital property. Thus at the beginning of any process of classifying spousal assets, everything is presumed to be marital property. When there is adequate proof to overcome the general presumption, then the proof will prevail and classification will be otherwise. But the "easy way," when there are no records or proof, will result in the operation of the presumption and in the classification of all spousal property as marital.

*The Present Interest:* A second building block is the creation of a *present* equal undivided interest for each spouse. This is a distinct departure from existing versions of "marital property" arising out of equitable distribution developments in family law. Those family-law interests set forth in marital property definitions in equitable distribution statutes are delayed-action in nature and come to maturity only during the dissolution process. Marital property under the Act is created *as assets are acquired* by the spouses, whether from income from the effort of either spouse during marriage, as income attributable to passive or investment sources, or as appreciation of or in an exchange for or rollover of existing marital property. When the assets are acquired from such sources, the incidents and attributes of marital property, including the creation of a present legal interest, attach simultaneously with the acquisition. The assets so acquired are instantly classified or characterized as marital property. The classification persists until the marriage terminates by dissolution or death, or until occurrence of a "reclassification" by one or another of the methods provided in the Act.

*The Income Rule:* The third feature is an income rule, creating an easily comprehended system. By treating all income from any source as marital property, the Act affords a simple and understandable arrangement. In the majority of marriages, most income will be spent sooner or later. In those so affluent that this does not

happen, the rule can either be followed or changed by a marital property agreement. In the latter group of marriages, some extra recordkeeping following an agreed bifurcation of income from marital and individual property should not pose an undue burden.

The income rule poses some "front-end" and "tail-end" problems. The "front-end" problem pertains to income received shortly after the determination date from effort or accrual of rights before the determination date. Actual ownership of such income became fixed before the determination date and it should not be and is not classified as marital property. This is handled by providing that income is marital only if "earned or accrued" after the determination date and during marriage.

With a disintegrating marriage in a state which has had the Act for a reasonable period of time, a cash basis or actual receipt rule at dissolution could give rise to significant abuses. This is the potential "tail-end" problem. Receipt of income under the management and control of one spouse could be delayed voluntarily until the dissolution was complete, to the prejudice of the former spouse who was not in such a position of control. Hence the earned or accrued rule of the Act also addresses this problem. The accounting and classification problems of the accrual or constructive receipt system used in the Act to deal with the tail-end problem obviously could necessitate tracing activities, but the potential for manipulation and diversion with a cash basis rule is such that the difficulty is justified.

*Transition to the Income Rule:* There is an additional important element in the treatment of income. All property of couples already married when the Act becomes law in an adopting state has a set of characteristics not created by the Act. The Act has been drafted to avoid altering those characteristics during the on-going marriage as far as the *principal* of the pre-adoption property is concerned. However the income rule obviously affects post-adoption income, classifying it as marital property. Post-adoption income is just that. It is not principal, and it is received and regulated by the Act's provisions only when the claim of right to it occurs by virtue of its having been earned or accrued after adoption. Hence the Act's income rule is not retroactive.

*Trusts:* Marital property transferred to a trust remains marital property and does not become "something else" under Subsection (e). A marital property agreement could provide otherwise. The subsection's principal enabling function is to permit the creation of revocable living trusts by one or both spouses without any automatic reclassification of property committed to the trust. If the trust is created by both spouses, or if created by one and consented to by the other, it would itself be a sufficient written form of marital property agreement to effect any reclassification directed by its terms if the other requirements of Section 10 are met. A trust created by one spouse would necessarily be measured by the good faith provisions of Section 2. The subsection would have no application to testamentary trusts, since marital property is the property of spouses. When a former spouse dies leaving a will that creates a trust, the property funding the trust can no longer be marital property. It could, and ordinarily would, be the decedent's share of *former* marital property.

*Appreciation of Individual Property:* Individual property definitions for post-determination date acquisitions are furnished in a listed format. In addition to such acquisitions by gift or inheritance, there are other obvious inclusions. One of special importance concerns *appreciation* of individual property. Assume that one spouse comes to a marriage subject to the Act as the owner of a valuable piece of real estate. It is individual property. If it quadruples in value, it is *still* individual property. While its income is marital property, the property itself and its appreciation in value is almost always individual property. One exception is the special rule announced in Section 14(b). That rule is concerned with the application to the individual property of one spouse of personal effort by the other spouse. It could apply in limited situations, but establishing it requires a very strong showing. Another possible exception could arise from mixing marital property with the individual property, also dealt with in Section 14. If the components of the mixed property can be traced, then no reclassification will occur. Monetary contributions to real estate acquisition or improvement are typically traceable, so that this form of reclassification regarding real estate should not be a frequent issue.

*Donated Property:* The rule treating property received by gift as individual property applies to gifts made to only one spouse. If a gift is made to both spouses, the donated property is marital property. This would apply to gifts to both in any form, including transfers to them as joint tenants, tenants in common, or in one of the title forms included in Section 11.

*Effect on Existing Property:* Subsection (h) states an important transitional rule. It can be assumed that in an adopting state one spouse might own property absolutely, and that a couple might also own property concurrently or as community property. The latter would be true of a couple which moved into an adopting state from one of the existing community property states as well as a couple in an adopting community property state. All of the property of a married couple in an adopting state on hand at the determination date would have a particular classification. Certain incidents would already have attached to the manner of

ownership. Survivorship would be an incident of jointly held or entireties property. A tenancy in common would consist of undivided interests, with each interest subject to individual rights of disposition. Community property would have the incidents described in the *Uniform Disposition of Community Property Rights at Death Act*, and possibly others developed between the spouses by agreement. Trust interests would be regulated by governing instruments. The Act is *not* designed to alter these various incidents of ownership or to reclassify such property.

With minor exceptions, the arrival of the determination date for such a couple would neither reclassify any of their property as marital property nor as any type of property other than what it was prior to the determination date. The exceptions all operate on that property only *after* the determination date. They are limited and include only the "deferred marital property" approach at dissolution and death set forth in Sections 17 and 18, the income treatment set forth in Subsection (d), and the specific provisions of Subsection (i).

Note that Subsection (h) applies to property of spouses owned before the determination date. On the other hand Subsection (f) deals specifically with property owned *before marriage* by persons marrying in an adopting state after the Act is effective. It follows the traditional pattern of community property and dissolution-based marital property statutes in clearly classifying solely owned property owned before marriage as individual property effective with the marriage. Except for its income, individual property under the Act is analogous to solely owned property in a common law state or to separate property in an American community property state. Texas, Louisiana and Idaho separate property is even more kindred, since the income of separate property in those states is community property.

*The "As If" Treatment:* Subsection (i) is a statutory statement to identify pre-determination date property that is solely owned as functioning with a "fraternal twin" relationship to individual property under the Act. It is a transitional rule, stated as it is to avoid a direct substantive reclassification of pre-determination date property, but to clarify the functional treatment of it in applying the Act. It is important that it be read as the "as if" rule that it is, and not as a reclassification statute.

The exceptions in Subsection (i) are intended to avoid any interference with actual ownership incidents in property owned prior to the determination date. For example, community property owned prior to the determination date should not be treated functionally as individual property in applying the Act. On the other hand, tenancy in common property could function as if it were individual property under the Act's provisions with each owner's undivided interest being treated as though it were individual property. A tenancy in common of individual property of the respective spouses is possible under the Act.

*Property "that is not marital property":* There are references in the Act to property of a spouse ".... that is not marital property ...." (Sections 8(b) and 14(a)); property ".... having any other classification ...." (Section 14(a)); ".... property of the designated owner of the policy ...." (Section 12(c)(4)); ".... all property then owned by the spouses .... which would have been marital property ...." (Section 17(1)); or ".... all property then owned by the spouse .... which would have been marital property ...." (Section 18(a)). It is reasonable to ask why such references are not to *individual* property and to ask further whether the Act fractionalizes all property of spouses into marital or individual property. The explanation is part of the transition problem and is consonant with Subsections (b) and (i). Property in existence prior to adoption is *not* individual property, by definition, since the classification of individual property is a creation of the Act. Property in existence prior to adoption of the Act is whatever it is without the Act. Subsection (h) makes it clear that the Act does not go about reclassifying that property. Hence there will be a multitude of couples that will have property that is "something else" than marital property or the individual property established by the Act. That "something else" type of property is property of a spouse that ".... is not marital property ...." property ".... having any other classification ...." and the like. Hence such descriptions are intentional in the reference they make to the "something else" or pre-determination date property to which they point.

#### SECTION 5. MANAGEMENT AND CONTROL OF PROPERTY OF SPOUSES.

(a) A spouse acting alone may manage and control:

- (1) that spouse's property that is not marital property;
- (2) except as provided in subsections (b) and (c), marital property held in that spouse's name alone or not held in the name of either spouse;
- (3) a policy of insurance if that spouse is designated as the owner on the records of the issuer of it;



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(4) the rights of an employee under an arrangement for deferred employment benefits that accrue as a result of that spouse's employment;

(5) a claim for relief vested in that spouse by other law; and

(6) marital property held in the names of both spouses in the alternative, including a manner of holding using the names of both spouses and the word "or."

(b) Spouses may manage and control marital property held in the names of both spouses other than in the alternative only if they act together.

(c) The right to manage and control marital property transferred to a trust is determined by the terms of the trust.

(d) The right to manage and control marital property does not determine the classification of property of the spouses and does not rebut the presumption of Section 4 (b).

(e) The right to manage and control marital property permits gifts of that property only to the extent provided in Section 6.

(f) The right to manage and control any property of spouses acquired before the determination date is not affected by this [Act].

(g) A court may appoint a [conservator, guardian] to exercise a disabled spouse's right to manage and control marital property.

#### Comment

*Title Based System:* If Section 4 is the heart of the Act, then Section 5 and its management and control system is its aorta. Management and control is a title based system and to that extent will parallel the management and control rights which typically follow title in common law states. However, there is a very basic difference. While title is virtually synonymous with ownership in the common law system, it is perhaps best understood as a *nominee* relationship under the Act. Title can be viewed as something of a permeable membrane that presents one state of affairs to third parties while encompassing an ownership relationship between the spouses within that relationship which may well be different from the title-side of the membrane. To lawyers long attuned to common law concepts of the impermeable membrane view of title, the thrust is a new one. A fairly useful illustrative analogy is the fractionalization of title which occurs when a trust is created. A trustee has "legal title" (and management rights) while a beneficiary (usually undisclosed on legal title) has equitable and beneficial rights. Two sets of rights coexist, yet the outside world need deal only with the trustee as apparent owner, notwithstanding the beneficiary's completely valid, enforceable, coexisting, but usually undisclosed rights. In the marital property situation, the spouses as co-owners are analogous to the beneficiaries and a spouse as sole holder of marital property is analogous to the trustee as title holder. This comment is *not* intended to imply that marital property creates a trust, but simply to use an analogy to illustrate the coexisting relationships that are present in both situations.

*Sole Management:* Under Section 5 either spouse has sole management and control rights of a marital property asset which that spouse "holds" alone. No joinder for management and control functions would be required for that property. Holding is defined in Section 1(9) and that definition and this Section function together to treat conventional title as the method of determining holding.

*Concurrent Holding:* Management and control of concurrently held assets is dealt with specifically. The rights are related to the use of "and" or "or" in the title. If "and" is used in the concurrent title, *both* spouses manage and control, and joinder of both is required to discharge management and control functions. If "or" is used, it means what it says, and either spouse may manage and control the asset. Section 11(c) effectively applies the provisions on management and control of concurrent property not only to the special optional forms authorized by Section 11, but to conventional forms already in use in adopting states.

Bearer property and other property not "held" can be managed and controlled by either spouse, and no joinder is required. (Section 5(a)(2)). Section 5(a)(2) permits a spouse to manage and control property not held in the name of either spouse; this covers bearer property. The term "held" in Section 1(9) does not extend to bearer property, and the provisions of Section 5(a)(2) integrate with that by permitting one spouse to manage and control any marital property that does not come within the purview of the holding definition in Section 1(9).

Special rules apply to insurance and employee benefits, and claims for relief. Insurance is managed and controlled by its owner. Employee benefits are managed and controlled by the employee on whose behalf they

accrue. A claim for relief is managed and controlled by the spouse in whom the claim is vested by other law. (Section 5(a)(3), (4) and (5)).

#### SECTION 6. GIFTS OF MARITAL PROPERTY TO THIRD PERSONS.

(a) A spouse acting alone may give to a third person marital property that the spouse has the right to manage and control only if the value of the marital property given to the third person does not aggregate more than [\$500] in a calendar year, or a larger amount if, when made, the gift is reasonable in amount considering the economic position of the spouses. Any other gift of marital property to a third person is subject to subsection (b) unless both spouses act together in making the gift.

(b) If a gift of marital property by a spouse does not comply with subsection (a), the other spouse may bring an action to recover the property or a compensatory judgment in place of the property, to the extent of noncompliance. The other spouse may bring the action against the donating spouse, the recipient of the gift, or both. The action must be commenced within the earlier of one year after the other spouse has notice of the gift or 3 years after the gift. If the recovery occurs during marriage, it is marital property. If the recovery occurs after a dissolution or the death of either spouse, it is limited to one-half of the value of the gift and is individual property.

#### Comment

Since each spouse has a present undivided ownership in marital property, unrestricted gifts of marital property to a third person by one spouse of property managed and controlled by that spouse could defeat the interest of the other spouse in the donated property. Section 6 deals with gifts to third persons by spouses who have sole management and control rights. It has an absolute safe-harbor provision permitting gifts of a specified dollar amount per year to one individual. The amount is bracketed and should be set at any level determined to be appropriate in an adopting state. It also has a less objective test of reasonableness with reference to the economic position of the spouses when made. The section has teeth in the form of a right of recovery. The section is specific in authorizing a recovery of only the portion of the gift that exceeds the permissible limit, rather than the entire gift. If the gift was of a specific item, the alternative recovery of a compensatory judgment is available to avoid awkward fractionalized ownership of such an item after the recovery action.

#### SECTION 7. PROPERTY TRANSACTIONS BETWEEN SPOUSES.

(a) Restrictions on the power of spouses to enter into property transactions with each other are abolished.

(b) Spouses may reclassify their property by gift or marital property agreement.

#### SECTION 8. OBLIGATIONS OF SPOUSES.

(a) An obligation incurred by a spouse during marriage, including one attributable to an act or omission during marriage, is presumed to be incurred in the interest of the marriage or the family.

(b) After the determination date:

(i) a spouse's obligation to satisfy a duty of support owed to the other spouse or to a child of the marriage may be satisfied only from all marital property and all other property of the obligated spouse that is not marital property;

(ii) an obligation incurred by a spouse in the interest of the marriage or the family may be satisfied only from all marital property and all other property of that spouse that is not marital property;

(iii) an obligation incurred by a spouse before or during marriage that is attributable to an obligation arising before marriage or to an act or omission occurring before marriage may be satisfied only from property of that spouse that is not marital property and that part of marital property which would have been the property of that spouse, but for the marriage; and

(iv) any other obligation incurred by a spouse during marriage, including one attributable to an act or omission during marriage, may be satisfied only from property of that spouse that is not marital property and that spouse's interest in marital property and in that order.

(c) This [Act] does not alter the relationship between spouses and their creditors with respect to any property or obligation in existence on the determination date.

(d) Provisions of a written consent signed by a creditor which diminish the rights of the creditor provided in this section are binding on the creditor.

(e) No provision of a marital property agreement adversely affects the interest of a creditor unless the creditor had actual knowledge of that provision when the obligation to that creditor was incurred. The effect of this subsection may not be varied by a marital property agreement.

(f) This [Act] does not affect the exemption of any property of spouses under other law.

#### Comment

**Basic Doctrine:** The section builds on a doctrine that has been developed and followed in Arizona, Louisiana and Washington. Ariz. Rev. Stat. Ann. Sec. 25-215 (1956); La. Rev. Civ. Code Ann. art. 2360; Wash. Rev. Code Ann. Sec. 26.16.205 (1974). See also McClanahan, *Community Property Law in the United States*, Sec. 10.4 (1982). The doctrine may be described as a "family purpose" doctrine, and it concerns the obligations incurred during the marriage and establishes a bifurcation separating those obligations that have a relation to the marriage, or the family, or the community, from those obligations incurred for the purely personal purposes of an incurring spouse. The Louisiana statute uses the terms ".... for the common interests of the spouses ...." in its definition of obligations having a relation to the marriage. The obligation having a relation to the marriage is treated in the three states as a community obligation. Obligations for personal purposes are treated as those of the incurring spouse, and that spouse's separate property is available to satisfy them, along with the spouse's interest in community property. See *Casper v. Valley Bank*, 28 Ariz. 373, 237 P. 175 (1925); *Garrett v. Shannon*, 13 Ariz. App. 332, 476 P.2d 538 (1970); *Beyers v. Moore*, 45 Wash. 2d 68, 272 P.2d 626 (1954).

The method used in the Act is to begin with a presumption. The same technique is used in Louisiana. La. Rev. Civ. Code Ann. art. 2361. An obligation incurred by a spouse during marriage is presumed to be incurred in the interest of the marriage or the family. The presumption specifically includes obligations arising out of an act or omission and thus covers the tort field. This is consistent with the development of the underlying family purpose doctrine. See *De Pinto v. Provident Security Life Ins. Co.*, 375 F.2d 50 (9th Cir. 1967); *McHenry v. Short*, 29 Wash. 2d 263, 186 P.2d 900 (1947); *McFadden v. Watson*, 51 Ariz. 110, 74 P.2d 118 (1938); *Benson v. Bush*, 3 Wash. App. 815, 502 P.2d 1245 (1972).

With the presumption as a background, the section proceeds to establish four categories of obligations with which a couple may be involved, and to clarify what property is available to satisfy those different categories of obligations.

**Support:** All marital property and all other property of the obligated spouse is available to satisfy an obligation of support owed to the other spouse or a child of the marriage.

**Family Purposes:** Obligations falling within the presumption, being for the interest of the marriage, may be satisfied from all marital property and from the property of the incurring spouse that is not marital property. See Comment to Section 4 for discussion of "property that is not marital property."

**Premarital Obligations:** A premarital obligation or an obligation incurred during marriage but attributable to an act or omission before marriage is to be satisfied from the property of the incurring spouse that is not marital property and from the marital property that would have been the property of the incurring spouse but for the marriage. This latter quantum of property is different from a spouse's undivided half-interest in marital property. Assume a marriage with only one spouse earning wages and assume that that spouse had a premarital obligation for child support of a child of a prior marriage. The obligation could be satisfied from any property of the obligated spouse that was not marital property. It could also be satisfied from the wages or the savings from the wages earned during the marriage. If marriage had not occurred, the wages would have been the solely owned property of the obligated spouse. Thus Subsection (b)(iii) renders all of those wages available, even though the wages would typically have created marital property. In the converse situation, if the obligation had been that of the spouse creating no wages, none of the employed spouse's wages, nor any marital property created with them, would be available for such an obligation. This prevents a windfall to the premarital creditor by a marriage, for no interest in marital property attributable to the effort of the new spouse of the obligated party becomes available to enhance the assets available to that creditor to satisfy a debt of the obligated spouse. The objective is that the marriage should be neutral as far as the premarital creditor is concerned, neither adding to nor detracting from the assets available for satisfaction of the claim.

*All Other Obligations:* Obligations not covered by the first three categories may be satisfied out of the property of the incurring spouse that is not marital property and from the interest of the incurring spouse in marital property. Subsection (b)(iv) specifically establishes the order of satisfaction by requiring that marital property should be reached after other property is exhausted. In this instance the marital property to be reached is the undivided one-half interest of the incurring spouse and is not the same as the property which the premarital creditor can reach. Under this fourth category would fall obligations incurred during marriage that were not incurred in the interest of the marriage or the family. See *de Elche v. Jacobsen*, 95 Wash. 2d 237, 622 P.2d 835 (1980).

The provisions of the section can be altered if a creditor is willing to diminish the rights established by the section. For example, one spouse with substantial amounts of individual property might wish to limit the possible obligation of the other spouse, even though the purpose of the obligation was clearly in the interest of the marriage. That spouse could obtain a writing from a creditor under Subsection (d) which would accomplish this. In the absence of it, Subsection (b)(ii) would subject the interest of the nonincurring spouse in marital property to the obligation. See N.M. Stat. Ann. Sec. 40-3-9A(4).

*Marital Property Agreements:* For purposes of a creditor's rights under the section, a marital property agreement may not redefine or reclassify marital property in a manner that has any adverse effect on the creditor unless the creditor had actual knowledge of the adverse provision when the credit was extended.

#### SECTION 9. PROTECTION OF BONA FIDE PURCHASERS DEALING WITH SPOUSES.

(a) In this section:

(1) "Bona fide purchaser" means a purchaser of property for value who: (i) has not knowingly been a party to fraud or illegality affecting the interest of the spouses or other parties to the transaction; (ii) does not have notice of an adverse claim by a spouse; and (iii) has acted in the transaction in good faith.

(2) "Purchase" means to acquire property by sale, lease, discount, negotiation, mortgage, pledge, or lien or otherwise to deal with property in a voluntary transaction other than a gift.

(3) A purchaser gives "value" for property acquired: (i) in return for a binding commitment to extend credit; (ii) as security for or in total or partial satisfaction of a pre-existing claim; (iii) by accepting delivery pursuant to a pre-existing contract for purchase; or (iv) generally, in return for any other consideration sufficient to support a simple contract.

(b) Notice of the existence of a marital property agreement, a marriage, or the termination of a marriage does not affect the status of a purchaser as a bona fide purchaser.

(c) Marital property purchased by a bona fide purchaser from a spouse having the right to manage and control the property under Section 5 is acquired free of any claim of the other spouse. The effect of this subsection may not be varied by a marital property agreement.

#### Comment

Third parties will deal with the spouse or spouses who manage and control, and that in turn depends on which spouse "holds" marital property. When one who satisfies the bona fide purchaser requirements deals with a spouse who has management and control rights under Section 5, the transaction is free from the claim of the other spouse. This section is one of three parts of the Act that cannot be altered by a marital property agreement. (Section 10(c)). Between the spouses, the section does not function to eliminate any claim, since it is addressed solely to the protection of bona fide purchasers. The definition of "purchase" follows UCC Sec. 1-201(32). The effect of a marital property agreement on a creditor is discussed in the Comment to Section 8.

#### SECTION 10. MARITAL PROPERTY AGREEMENT.

(a) A marital property agreement must be a document signed by both spouses. It is enforceable without consideration.

(b) A marital property agreement may not adversely affect the right of a child to support.

(c) Except as provided in Sections 2, 8 (e), and 9 (c) and in subsection (b), in a marital property agreement spouses may agree with respect to:

(1) rights and obligations in any of their property whenever and wherever acquired or located;

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- (2) management and control of any of their property;
  - (3) disposition of any of their property on dissolution, death, or the occurrence or nonoccurrence of any other event;
  - (4) modification or elimination of spousal support;
  - (5) making a will, trust, or other arrangement to carry out the agreement;
  - (6) a provision that upon the death of either of them, any of their property, including after-acquired property, will pass without probate to a designated person, trust, or other entity by nontestamentary disposition;
  - (7) choice of law governing construction of the agreement; and
  - (8) any other matter affecting their property not in violation of public policy or a statute imposing a criminal penalty.
- (d) A marital property agreement may be amended or revoked only by a later marital property agreement. The amended agreement or the revocation is enforceable without consideration.
- (e) Persons intending to marry each other may enter into a marital property agreement as if married, but the agreement becomes effective only upon their marriage.
- (f) A marital property agreement executed during marriage is not enforceable if the spouse against whom enforcement is sought proves that:
- (1) the agreement was unconscionable when made; or
  - (2) that spouse did not execute the agreement voluntarily; or
  - (3) before execution of the agreement, that spouse:
    - (i) was not provided a fair and reasonable disclosure of the property or financial obligations of the other spouse;
    - (ii) did not voluntarily sign a written consent expressly waiving any right to disclosure of the property or financial obligations of the other spouse beyond the disclosure provided; and
    - (iii) did not have notice of the property or financial obligations of the other spouse.
- (g) A marital property agreement executed before marriage is not enforceable if the spouse against whom enforcement is sought proves that:
- (1) that spouse did not execute the agreement voluntarily; or
  - (2) the agreement was unconscionable when made and before execution of the agreement that spouse:
    - (i) was not provided a fair and reasonable disclosure of the property or financial obligations of the other spouse;
    - (ii) did not voluntarily sign a written consent expressly waiving any right to disclosure of the property or financial obligations of the other spouse beyond the disclosure provided; and
    - (iii) did not have notice of the property or financial obligations of the other spouse.
- (h) An issue of unconscionability of a marital property agreement is for decision by the court as a matter of law.
- (i) If a provision of a marital property agreement modifies or eliminates spousal support and that modification or elimination causes one spouse to be eligible for support under a program of public assistance at the time of dissolution, the court may require the other spouse to provide support to the extent necessary to avoid that eligibility, notwithstanding the terms of the agreement.
- (j) A document signed before the effective date of this [Act] by spouses or unmarried persons who subsequently married each other which affects the property of either of them and is enforceable by either of them without reference to this [Act] is not affected by this [Act] except as provided otherwise in a marital property agreement made after the determination date.

**Comment**

The Act provides almost unlimited contractual freedom for persons who want to amend, avoid or adopt its provisions. This is codified in this section. An important characteristic of a marital property agreement is that

it will usually be a postmarital agreement. On the other hand, a premarital agreement precedes the marriage by definition. Conceptually, the typical attitude toward a premarital agreement is that it will be changed infrequently after the marriage, if at all. On the other hand, the approach in this Act toward marital property agreements is that there may, and usually will, be many of them made at numerous times during a marriage. Section 10(e) specifically sanctions entry into a marital property agreement before marriage, but provides that it becomes effective only upon marriage of the parties to it. If they do not marry, the agreement would be a nullity.

**Multiple Agreements:** A number of separate and distinct marital property agreements might be in existence in a given marriage. In adopting states, spouses would be able to execute as many of these agreements as needed during their marriage. The policy announced by the section is that any arrangement that changes the application of the Act should be a marital property agreement. In turn it should conform with Section 10.

**Scope:** The specific group of matters which a marital property agreement can cover, set out in Subsection (c), is not exclusive. Paragraph 8 of the subsection extends the opportunity for contracting between spouses to any other matters not in violation of public policy or any statute imposing a criminal penalty.

**Enforceability:** There are two sets of provisions regarding enforceability. One is parallel to the *Uniform Premarital Agreements Act*. (Subsection (g)). These provisions apply to marital property agreements made before marriage. The second set of provisions applies to marital property agreements made after marriage. (Subsection (h)). The postmarital requirements elevate the test of "unconscionable when made" as a disqualifying factor. In the postmarital agreement an agreement may not be enforced against a spouse who proves that the agreement was unconscionable when made.

Although the Act sets forth a specific group of requirements for enforceability, they are not exclusive. Ordinary contract defenses not specifically ruled out by the Act (as lack of consideration is) remain available.

**Dispositions At Death:** Paragraph 6 of Subsection (c) contains provisions substantially similar to those in Washington law. Wash. Rev. Code Ann. Sec. 26.16.120 (1974). These have been in effect in Washington since 1881, and they constitute a valuable and useful method of nonprobate disposition. The language in the Act contains after-acquired property provisions. It is intended to be used on an omnibus basis with respect to all property, or on a more limited basis with respect to a specified asset or group of assets. It constitutes a statutory authorization for a disposition other than one under the Statute of Wills. In that respect, it also follows certain of the policies announced in Section 6.201 of the *Uniform Probate Code*, although the latter is seen by many as being drafted to apply on an asset-by-asset basis rather than on the omnibus basis available in Subsection (c)(6). It should be noted that since the provisions of this type of agreement are incorporated in a marital property agreement, they may not be altered unilaterally. A discussion of the use of the agreements in Washington appears in Cross, *The Community Property Law of Washington*, 49 Wash. L. Rev. 729, 798, 805 (1974). A version of the arrangement in use in another state can be found in Idaho Code Sec. 15-6-201 which incorporates the idea into Idaho's version of Sec. 6.201 of the *Uniform Probate Code*. See also Bell, *Statutory Survivorship Contracts in the State of Washington*, 1 Community Prop. J. 239 (1974); Note, *The Community Property Agreement: A Probate Cure With Side Effects*, 18 Gonz. L. Rev. 121 (1983); Note, *A First Look at the Community Property Agreement in Idaho*, 12 Idaho L. Rev. 41 (1975).

**No Consideration Required; Formalities:** No consideration is required for a marital property agreement, and the agreement, amendments, and revocations of the agreement require the signature of both spouses. Subsection (d) relates to amendments and revocations and requires that these be by later marital property agreements. These would necessarily be documents signed by both spouses, since Subsection (a) requires that all marital property agreements be signed by both spouses.

**Existing Agreements:** Subsection (j) deals with a transitional problem. From the point of view of comprehensibility and ease of administration, it would be desirable to convert agreements relating to the subject matter of the Act to marital property agreements under the Act with the adoption of the Act. However, such legislation could be seen as impairing the obligation of those agreements and as retroactive, and it is therefore avoided. Thus a predetermination date agreement dealing with subject matter such as that in the Act will simply continue to stand on such authority as it had without the Act, and the Act neither helps nor hinders that agreement.

**SECTION 11. OPTIONAL FORMS OF HOLDING PROPERTY, INCLUDING USE OF "AND" OR "OR" SURVIVORSHIP OWNERSHIP.**

(a) Spouses may hold marital property in a form that designates the holders of it by the words "(name of one spouse) or (name of other spouse) as marital property." Marital property held in that form is subject to Section 5 (a) (6).

(b) Spouses may hold marital property in a form that designates the holder of it by the words "(name of one spouse) and (name of other spouse) as marital property." Marital property held in that form is subject to Section 5 (b).

(c) A spouse may hold individual property in a form that designates the holder of it by the words "(name of spouse) as individual property." Individual property held in that form is subject to Section 5 (a) (1).

(d) Spouses may hold property in any other form permitted by law, including a concurrent form or a form that provides for survivorship ownership.

(e) If the words "survivorship marital property" are used instead of the words "marital property" in the form described in subsection (a) or (b), marital property so held is survivorship marital property. On the death of a spouse, the ownership rights of that spouse in survivorship marital property vest solely in the surviving spouse by nontestamentary disposition at death. The first deceased spouse does not have a right of disposition at death of any interest in survivorship marital property. Holding marital property in a form described in subsection (a) or (b) does not alone establish survivorship ownership between the spouses with respect to the property held in that form.

**Comment**

Although the provisions of the Act do not require any particular form of labeling or title-documented property, that kind of labeling will be desirable in an adopting state. For a couple wishing to be specific and definite with respect to the classification of property, the labeling device provided by the section is a desirable provision for holding property.

*Relationship to Management and Control:* The section goes beyond mere labeling and provides specific confirmation of management and control rights with respect to types of labeling which are congruent with Section 5. Use of the Act's designation of property as marital property in a conjunctive or a disjunctive form will have different effects on management and control rights. The conjunctive ("and") form will require management and control by both spouses and joinder of both in transactions affecting the property. The disjunctive ("or") form permits management and control by either spouse without the necessity of joinder by the other.

*Other Forms:* Affirmative recognition of the ability to hold marital property in any form permitted by other law is provided by Subsection (d). This is consistent with the underlying difference under the Act between ownership and the integrated matters of title or holding and management and control.

*Survivorship Ownership:* An important substantive addition made by the section is a survivorship ownership feature. If the appropriate words described in the section are added to the designation by which the property is held, then survivorship ownership will follow that. If those words are not used, there is a specific statement that survivorship is not achieved by using the marital property form in either the conjunctive or the disjunctive form. It is important to note that survivorship marital property can be created with respect to marital property held in either the disjunctive form or the conjunctive form. This feature creates a wider option than would be afforded by limiting survivorship to the disjunctive form only. Management and control rights are unaffected by the addition of the survivorship language and relate back to the provisions in the last sentences of Subsections (a) and (b). The survivorship estate is not a form of joint tenancy but is a new statutory estate created by the section. It is not intended to carry on the arcane doctrines of joint tenancy but simply to establish a nonprobate survivorship incident by the utilization of the appropriate words on a document of title or other medium by which property is held. It is consistent with the policy of Section 10(c)(6) and Section 6.201 of the *Uniform Probate Code*.

An adopting state will wish to review banking statutes dealing with concurrent ownership rights to assure appropriate recognition of the provisions of the section and coordination with existing provisions of banking statutes.

## SECTION 12. CLASSIFICATION OF LIFE INSURANCE POLICIES AND PROCEEDS.

## (a) In this section:

(1) "Owner" means a person appearing on the records of the policy issuer as the person having the ownership interest or, if no person other than the insured appears on those records as a person having that interest, it means the insured.

(2) "Ownership interest" means the rights of an owner under a policy.

(3) "Policy" means an insurance policy insuring the life of a spouse and providing for payment of death benefits at the spouse's death.

(4) "Proceeds" means the death benefit from a policy and all other economic benefits from it, whether they accrue or become payable as a result of the death of an insured person or upon the occurrence or nonoccurrence of another event.

(b) If a policy issuer makes payments or takes actions in accordance with the policy and the issuer's records, the issuer is not liable because of those payments or actions unless, at the time of the payments or actions, it had actual knowledge of inconsistent provisions of a decree or marital property agreement or of an adverse claim by a spouse, former spouse, surviving spouse, or persons claiming under a deceased spouse's disposition at death.

## (c) Except as provided in subsections (d), (e), and (f):

(1) The ownership interest and proceeds of a policy issued after the determination date which designates the insured as the owner are marital property without regard to the classification of property used to pay premiums on the policy.

(2) The ownership interest and proceeds of a policy issued before the determination date which designates the insured as the owner are mixed property if a premium on the policy is paid from marital property after the determination date without regard to the classification of property used to pay premiums on that policy after the initial payment of a premium on it from marital property. The marital property component of the ownership interest and proceeds is the part resulting from multiplying the entire ownership interest and proceeds by a fraction of which the numerator is the period during marriage that the policy was in effect after the date on which a premium was paid from marital property and the denominator is the entire period the policy was in effect.

(3) The ownership interest and proceeds of a policy issued during marriage which designates the spouse of the insured as the owner are individual property of its owner without regard to the classification of property used to pay premiums on the policy.

(4) The ownership interest and proceeds of a policy that designates a person other than either of the spouses as the owner are not affected by this [Act] if no premium on the policy is paid from marital property after the determination date. If a premium on the policy is paid from marital property after the determination date, the ownership interest and proceeds of the policy are in part property of the designated owner of the policy and in part marital property of the spouses without regard to the classification of property used to pay premiums on that policy after the initial payment of a premium on it from marital property. The marital property component of the ownership interest and proceeds is the part resulting from multiplying the entire ownership interest and proceeds by a fraction of which the numerator is the period during marriage that the policy was in effect after the date on which a premium was paid from marital property and the denominator is the entire period the policy was in effect.

(5) Written consent by a spouse to the designation of another person as the beneficiary of the proceeds of a policy is effective to relinquish that spouse's interest in the ownership interest and proceeds of the policy without regard to the classification of property used by a spouse or another to pay premiums on that policy. A designation by either spouse of a parent or child of either of the spouses as the beneficiary of the proceeds of a policy is presumed to have been made with the consent of the other spouse.



(6) Unless the spouses provide otherwise in a marital property agreement, designation of a trust as the beneficiary of the proceeds of a policy with a marital property component does not reclassify that component.

(d) This section does not affect a creditor's interest in the ownership interest or proceeds of a policy assigned or made payable to the creditor as security.

(e) The interest of a person as owner or beneficiary of a policy acquired under a decree or property settlement agreement incident to a prior marriage or parenthood is not marital property without regard to the classification of property used to pay premiums on that policy.

(f) This section does not affect the ownership interest or proceeds of a policy if neither spouse is designated as an owner in the policy or the records of the policy issuer and no marital property is used to pay a premium on the policy.

#### Comment

This section sets forth a series of rules regarding the classification of life insurance policies and the proceeds of them.

As with other provisions of the Act, it is important to review the section with an awareness that a marital property agreement can change its provisions.

*Protected Parties:* A series of definite rules operating on described objective facts protects certain parties to insurance policy transactions. The first protected party is the issuing insurance company. Subsection (b) relieves it from liability if it proceeds on the basis of the policy and its own records unless it has *actual knowledge* of other facts which would affect claims under the policy or those records.

The second protected party is a creditor to whom a policy is assigned or made payable. Subsection (d) provides that the section does not affect that creditor's interest in the policy, so that its provisions do not concern or impair the rights of the creditor.

The third protected party is a person who is an owner or beneficiary by virtue of provisions made in the dissolution of a prior marriage or as an incident to parenthood. In many dissolutions the maintenance of a life insurance policy for children of the marriage or for a former spouse is required. Subsection (e) accords to persons intended to be benefited from that type of provision protection from the other provisions of the section.

Finally, Subsection (f) provides that if neither spouse is an owner of a policy and no marital property is used to pay a premium on the policy, the section will have no effect on the policy or its proceeds. Thus, a typical business-based life insurance policy would ordinarily be unaffected by any provision of the section. Similarly, insurance owned and paid for by a child on the life of a parent would be unaffected by the section.

Carving out those four groups of protected persons leaves six separate situations with which the section deals.

*The Basic Rule:* The basic rule is found in Subsection (c)(1). If a policy is issued *after the determination date* and an insured spouse is the owner, it is a marital property policy, *without regard to the source of premium payments*. This situation is the typical garden-variety transaction in which one spouse is the owner of a policy on his or her life. The section offers a rule of comparative simplicity for that policy — it is marital property.

*Straddles:* The next situation dealt with is a "straddle." Subsection (c)(2) speaks of a policy that existed before the determination date which is owned by the insured and continues in force after the determination date. Payment of *any* premium on such a policy at any time *after* the determination date will operate as a reclassification of the policy ownership and proceeds. A formula is set forth in the section to establish the marital property component.

*Spouse-Owned Insurance:* Under Subsection (c)(3), the frequently used transaction of spouse-owned insurance is treated. The Act assumes that a designation of a spouse of an insured as an owner will typically be used if the parties desire that the non-insured spouse be the owner for all purposes. The effect of the Act is to perfect that treatment. While the spouses could always agree to an alternative treatment, unless they do, a policy owned by one on the life of the other will be individual property of the owner without regard to the source of premium payments.

*Third Person Ownership:* A fourth situation, dealt with in Subsection (c)(4), concerns a policy owned by third persons with premiums paid from marital property. The "straddle" system and accompanying formula is

used to deal with the ownership interest and proceeds. The straddle is again initiated by the first payment of a premium from marital property.

*Parent or Child as Beneficiary:* Subsection (c)(5) presents a means of relinquishing marital property interests in life insurance and contains a presumption that the designation by a spouse of a parent or a child of either spouse as a beneficiary is made with the consent of the other spouse.

*Trust As Beneficiary:* The marital property component of a policy retains that classification even if a trust is designated as a beneficiary under Subsection (c)(6). Consent of both spouses to another classification is possible to alter this result.

### SECTION 13. CLASSIFICATION OF DEFERRED EMPLOYMENT BENEFITS.

(a) A deferred employment benefit attributable to employment of a spouse occurring after the determination date is marital property.

(b) A deferred employment benefit attributable to employment of a spouse occurring during marriage and partly before and partly after the determination date is mixed property. The marital property component of that mixed property is the part resulting from multiplying the entire benefit by a fraction of which the numerator is the period of employment giving rise to the benefit that occurred after the determination date and during marriage and the denominator is the total period of the employment. Unless provided otherwise in a decree, marital property agreement, or written consent, valuation of a deferred employment benefit that is mixed property shall be made as of the death of a spouse or a dissolution.

(c) Ownership or disposition provisions of a deferred employment benefit which conflict with subsections (a) and (b) are ineffective between spouses, former spouses, or between a surviving spouse and a person claiming under a deceased spouse's disposition at death.

(d) If an administrator of an arrangement for deferred employment benefits makes payments or takes actions in accordance with the arrangement and the administrator's records, the administrator is not liable because of those payments or actions unless, at the time of the payments or actions, it had actual knowledge of inconsistent provisions of a decree or marital property agreement or of an adverse claim by a spouse, former spouse, surviving spouse, or a person claiming under a deceased spouse's disposition at death.

#### Comment

This section deals with marital property rights in employment benefits. Its provisions may be varied by a marital property agreement.

*Protection:* As with the payment of life insurance proceeds under Section 12, Subsection (d) protects an entity which makes payments in accordance with the employee benefit plan and its own records. Unless it has actual knowledge that a decree or marital property agreement requires some other payment, or actual knowledge of an adverse claim by a spouse or surviving spouse, that entity has no liability even though its payments may be inconsistent with such rights or claims.

*The Two Formats:* The section deals with two situations. A deferred employment benefit attributable to employment after the determination date is marital property under Subsection (a). Such a benefit attributable to employment during marriage and before and after the determination date is subject to a formula which uses time periods.

*The Array of Problems:* There are many significant and important problems regarding employee benefits which the Act does not address specifically. As a property statute, the thrust of the Act is to treat an appropriate quantum of an employee benefit as marital property. From that point on, a court dealing with the matter will have before it the many other problems in the field. These include valuation problems, questions regarding the time at which an interest is to be quantified and delivered, questions relating to whether the plan is or is not in pay status, problems with respect to events affecting the plan which can occur with the passage of time, federal preemption problems, problems with respect to the claims of prior spouses, and many other problems that are now being heard on a daily basis in courts throughout the nation. See 3 *Equitable Distribution Rep.* 109 (Special Pension Issue, April 1983); McClanahan, *Community Property Law in the United States*, Sec. 12.15 (1982); O'Neill, *Pensions As Marital Property: Valuation, Allocation and Related Mysteries*, 16 Creighton L. Rev. 743 (1983); Campbell, *Pension Plan Benefits as an Asset in Dissolution-of-Marriage Cases*,

61 Taxes 583 (1983); *Kalinowski v. Kalinowski*, 9 Fam. L. Rep. 3033 (Pa. Ct. of Comm. Pl. 1983). There is no consensus in the existing state of the law that justifies the formulation of more than the general policy in the section. Adopting states will already have dealt with many of these problems and the Act does not alter that case law, but simply operates to establish an appropriate marital property interest. The existing body of state case law may be applied to that property interest.

Some federal benefit programs, such as the Railroad Retirement Act (45 U.S.C. Sec. 231 *et seq.*), preempt state definitions of property which include pension benefits in dissolution property settlements. *Hisquierdo v. Hisquierdo*, 439 U.S. 572 (1979). See also *Fritz v. Railroad Retirement Board*, 449 U.S. 166 (1980). Where there is federal preemption former spouses may themselves qualify as independent beneficiaries. In the case of the Railroad Retirement Act, see 45 U.S.C. Sec. 231a (c)(4) (divorced spouse annuity), and 45 U.S.C. Sec. 231a (d)(1)(v) (surviving divorced wife). See also the Uniform Services Former Spouses' Protection Act, 10 U.S.C. Sec. 1408, reversing the United States Supreme Court decision in *McCarty v. McCarty*, 453 U.S. 210 (1981), and enacting into law a time period formula bearing some analogy to that used in the section. The preemption problem exists independently of the Act, and obviously cannot be solved by actual or proposed state legislation in any event. See Reppy and Samuels, *Community Property in the United States*, p. 396 ff (1982).

#### SECTION 14. MIXED PROPERTY.

(a) Except as provided otherwise in Sections 12 and 13, mixing marital property with property having any other classification reclassifies the other property to marital property unless the component of the mixed property which is not marital property can be traced.

(b) Application by one spouse of substantial labor, effort, inventiveness, physical or intellectual skill, creativity, or managerial activity on individual property of the other spouse creates marital property attributable to that application if:

(i) reasonable compensation is not received for the application; and

(ii) substantial appreciation of the individual property of the other spouse results from the application.

#### Comment

Commingleing of the assets of spouses is an everyday occurrence without the Act, and will continue with or without it. The Act supplies a rule to deal with it. Under that rule, mixing properties that cannot be identified or traced after the mixing will result in a reclassification. Since the general presumption of Section 4 (b) operates to classify all spousal property as marital property, that will be the result in the absence of the ability to trace.

*Tracing:* The basic rule of Section 14 requires a tracing in order to "unmix" property. In turn the tracing would necessarily be done under the appropriate tracing rules of an adopting state. See McClanahan, *Community Property Law in the United States*, Secs. 6.7 and 6.8 (1982) and Reppy and Samuels, *Community Property in the United States*, Chapter 10 (1982), for discussion of tracing principles. U.C.C. Sec. 9-306 also supplies a version of tracing rules. The policy of the Act is to enhance the procedures and practices which create marital property. Consequently this section would have the effect of treating mixed property as marital property unless tracing was a possibility.

*What of De Minimis Mixing?* An obvious matter of concern is the possibility of serious injustice that could result from mixing a minimal amount of marital property with a substantial amount of other property. See Reppy and Samuels, *Community Property in the United States*, p. 128 ff (1982). For example, one principal payment might be made from marital property on a large mortgage on a valuable piece of individual real property. This would mix marital and individual property. Another example might be one deposit of marital property to a very large individual bank account. However these types of transactions lend themselves to solution by an application of tracing, since the underlying types of property are very much record-oriented. Meeting the burden of proof in a tracing process from the records should usually be possible.

A more difficult case is that of fungible properties — a large stamp, coin or precious gem collection, for example. These will create the same types of problems that they already create when they are not in unified ownership. Commingleing of fungible goods without being willing to sacrifice ownership is a highly dangerous practice and would remain so under the Act. In reality the spouse who stands to gain from a reclassification arising from a "tainting" of a large collection of fungibles with a small amount of marital property will have to carry the burden of proving that a mixing even occurred. In a sense that imposes the burden on that spouse to

trace the marital property *into* the mixed property, which will be an effective though backward threshold method of tracing.

**Commingled Accounts:** Commingled accounts (such as bank accounts and mutual fund accounts to which continuing payments for new purchases are made) and increased value resulting from payments on liens on property are examples of types of mixed property which will undoubtedly occur and which will typically require solutions. Those problems and solutions for them already exist in dissolution and probate matters. The Act would necessarily build on the procedures for tracing that exist in an adopting state. In addition, accounts of that type are frequently accompanied by normal and routine documentation and records which would ease the tracing process.

One rather common mixing process will undoubtedly occur. Many bank accounts, mutual fund accounts and common-stock dividend reinvestment programs provide automatic reinvestment of dividends and interest. Under the Act, income is marital property. Hence the automatic reinvestment of income will be a mixing of marital property with other property if the accounts or common stock are not already marital property. Under the section this will reclassify the accounts or common stock to marital property absent tracing. Spouses wishing to avoid this result could avoid automatic reinvestment of dividends or interest in such programs or could create an individual property classification for the reinvested income by a marital property agreement.

**Physical Labor:** The section deals with another extremely important issue. It is the situation arising from the application to the individual property of one spouse of personal effort by the other spouse and carrying the burden of proving its elements will be difficult. The rule of the section is strict. It articulates a bias against creation of marital property from such an act unless the effort has been substantial and has been responsible for substantial appreciation. Routine, normal, and usual effort is not substantial. Though drawing a precise line as to what is substantial and what is not is not possible, the section does not create opportunity to translate for recognizing minimal effort to a property interest. The section is only satisfied by proof of (1) a truly substantial effort followed by (2) a truly substantial appreciation *attributable to the effort* for which (3) no reasonable compensation was received. Many situations can be visualized. Real property transactions are those in which the problem will typically occur. One spouse will bring real property into the marriage. After the marriage, that real property will be an important element in the economic life of the couple. The other spouse will improve it by physical labor. This might be work on a farm, or improvements or additions to a home or to a piece of commercial real estate. The statute operates to avoid the creation of marital property if reasonable compensation for the effort was paid at the time that it occurred. If the compensation was nominal or nonexistent, then the provisions of the section still require a showing that the effort was substantial and that substantial appreciation resulted from it. Otherwise there can be no quantification of the marital property created by the effort and the spouse expending the effort will simply have done so without anything demonstrable to show for it.

**What is the Laborer's Right?** Section 14(b) provides that the physical labor creates *marital property* when it is applicable. That would mean that the right of the spouse who created the marital property is to an interest in the asset, and not to a right of reimbursement or a lien for a specific amount. As the marital property component rises and falls in value, the interest rises and falls.

**Burden of Proof:** Many mixing problems that might otherwise exist will be resolved by burden of proof requirements. A spouse claiming a particular classification for an asset contrary to the general presumption of Section 4(b) will have the burden of proof on that claim, and failure to meet it would render any mixing issue moot. In particular meeting the burden of proof should be helpful in the *de minimus* mixing situations, since proving mixing, even of small amounts, is itself a form of tracing.

#### SECTION 15. INTERSPOUSAL REMEDIES.

(a) A spouse has a claim against the other spouse for breach of the duty of good faith imposed by Section 2 resulting in damage to the claimant spouse's present undivided one-half interest in marital property.

(b) A court may order an accounting of the property and obligations of the spouses and may determine rights of ownership in, beneficial enjoyment of, or access to, marital property and the classification of all property of the spouses.

(c) A court may order that the name of a spouse be added to marital property held in the name of the other spouse alone, except with respect to:

- (1) a partnership interest held by the other spouse as a general partner;

- (2) an interest in a professional corporation, professional association, or similar entity held by the other spouse as a stockholder or member;
  - (3) an asset of an unincorporated business if the other spouse is the only spouse involved in operating or managing the business; or
  - (4) any other property if the addition would adversely affect the rights of a third person.
- (d) Except as provided otherwise in Section 6 (b), a spouse must commence an action against the other spouse under subsection (a) not later than 3 years after acquiring actual knowledge of the facts giving rise to the claim.

#### Comment

The section will create a change in the law of those states which prohibit litigation between spouses regarding property rights during an ongoing marriage. Since the Act creates respective vested interests in marital property while still permitting individual management and control of that property, there is an obvious possibility that management and control rights could be exercised in a way that damages or eliminates the interest of the spouse who does not hold the property. This section creates a remedy for this type of conduct. An important purpose of the section is creation of a remedy for a violation of the good faith responsibility between spouses required by Section 2. See McClanahan, *Community Property Law in the United States*, Sec. 9.12 (1982); Reppy and Samuels, *Community Property in the United States*, p. 243 ff (1982); Comment, *California's New Community Property Law — Its Effect On Interspousal Mismanagement Litigation*, 5 Pac. L.J. 723 (1974). It also affords a remedy for violations of specific provisions contained throughout the Act. However, it is not intended to reverse interspousal immunity beyond its terms unless an adopting state should choose to do so. Note that Section 6, dealing with gifts, also creates rights for one spouse to proceed against the other spouse. Those rights are in addition to the provisions of this section.

*The Basis:* The rationale of the section is well explained in De Funiak and Vaughn, *Principles of Community Property*, Sec. 151 (1971). There it is pointed out that in community property jurisdictions

“... it must follow as a logical result that each is entitled to protect or enforce against the other his or her rights in the common property or to enforce or protect as against the other his or her rights in separate property, even by civil action .... the common law fiction that husband and wife are one person, so that one cannot sue the other during coverture, is alien to the community property system's view of the spouses as individuals in their own right .... if this right to sue did not exist, one spouse, especially if the title to the property were in his or her name, might be enabled to appropriate community property to his or her own use or otherwise deny or injure the rights therein of the other spouse without the other spouse having any remedy whereby to defeat such conduct.”

*Accounting:* The accounting remedy contemplated is a form of balancing of the property rights between the spouses. It is not intended that such an accounting would be the classic fiduciary accounting in either style or substance. In particular, it is not intended that such an accounting should prevent the balancing of losses and gains or that it should charge one spouse with losses while not crediting gains. Rather, the accounting would simply establish what is marital property and what is not. If an “unmixing” under Section 14 was appropriate, that would be accomplished in the accounting. In addition to the accounting, the rights of the spouses by way of ownership or beneficial enjoyment of or access to marital property or other property is a contemplated form of relief under the Act. The remedy could well include some form of separation of property if needed to protect the ownership or beneficial enjoyment of the spouses in any of their property. See Reppy and Samuels, *Community Property in the United States*, p. 247 ff (1982).

*“Add-A-Name”:* One of the ways in which a spouse's interest could be injured would follow utilization of a one-spouse method of holding property and management or disposition of that property to the prejudice of the other spouse. In order to prevent this, the section has a specific provision for adding the name of a spouse to the form in which marital property is held. However, this procedure has certain safeguards and prohibitions. The “add-a-name” function cannot occur with respect to general partnership interests, professional entities, unincorporated businesses operated by the other spouse, or other property if a third party's interests would be adversely affected.

*Statute of Limitations:* The section contains a statute of limitations. This is intended to function as a means of clearing the records. It operates in a manner similar to that used in fraud-type statutes of limitations. The time period runs only after actual knowledge of facts which would give rise to a claim. If there is a dissolution or death, the statute of limitation provisions would be subject to an adopting state's limiting provisions for

actions between parties to a dissolution and for claims against an estate set out in its dissolution and probate statutes.

If the statute of limitations operates during the course of a marriage to bar any actions, that bar will be in effect at death or dissolution. That could mean frustration in some circumstances, so that consideration of enforcement of rights under the section during the course of a marriage will be appropriate.

While it is not the purpose of the section to open the door to a torrent of interspousal "economic fault" litigation, it is nonetheless necessary to provide remedies for conduct that injures the interest of one of the spouses. The dominant theme of the relationship between the spouses toward their property is established by the good faith requirement of Section 2. As stated in the comment to that section, a spouse is not bound to succeed in an economic sense. An appropriate regard for the property interests of the other spouse and an avoidance of an unfair advantage are the norm under the good faith requirement. This section provides a remedy for interference or damage. If that can be proven, particularly against an allegation of good faith conduct by the other spouse, a remedy is appropriate. However, such matters should not be dredged up after the apparent ratification that would be implied by the passage of time. The specific statute of limitations has been added for that reason and in order to operate as something of a "cleansing" process in matters of marital economics.

#### SECTION 16. INVALID MARRIAGES.

If a marriage is invalidated by a decree, a court may apply so much of this [Act] to the property of the persons who were parties to the invalid marriage as is necessary to avoid an inequitable result.

##### Comment

The section should be read with Sections 208 and 209 of the *Uniform Marriage and Divorce Act* dealing with declarations of invalidity and putative spouses. Adopting states should also review their annulment provisions if they do not follow Section 208. The section is intended to deal only with spousal relations and not with unmarried cohabitation.

#### SECTION 17. TREATMENT OF CERTAIN PROPERTY AT DISSOLUTION.

Except as provided in Section 16:

(1) In a dissolution, all property then owned by the spouses that was acquired during marriage and before the determination date which would have been marital property under this [Act] if acquired after the determination date must be treated as if it were marital property.

(2) In a dissolution, any property of either spouse which can be traced to property received by a spouse after the determination date as a recovery for a loss of earning capacity during marriage must be treated as if it were marital property.

(3) After a dissolution, each former spouse owns an undivided one-half interest in the former marital property as a tenant in common except as provided otherwise in a decree or written consent.

[(4) In an action for legal separation, the court may decree the extent to which property acquired by the spouses after the legal separation is marital property and the responsibility of each spouse for obligations incurred after the decree of legal separation.]

##### Comment

The Act contains no provision which would make an immediate alteration in the classification of the property of couples to which it becomes applicable who had married before its effective date. See Comment to Section 4. That property will continue to have whatever characteristics it had before the Act became applicable to its owners. The policy reason for this approach is avoidance of constitutional problems which would attend any effort to alter existing rights in property acquired before the Act was effective.

*The Concept of Deferral:* To that extent, the Act parallels procedures followed when states adopt changes in intestate share and forced heirship provisions or changes which create equitable distribution structures to apply at dissolution. Such changes make no *immediate* change in the rights in property which existed at the time the changes become effective. However, with respect to all of that existing property, as well as property acquired after the statutory change, when a time of dissolution is subsequently reached, such statutes typically create a state-authorized system of division and disposition which is applied to that property. It is accepted that a state has an appropriate role in determining the disposition of property at dissolution. It has also been settled that provisions in state dissolution property settlement statutes can affect not only property which came

into being after those statutes were enacted, but property which came into being before that. *Kujawinski v. Kujawinski*, 71 Ill. 2d 563; 376 N.E. 2d 1382 (1978); *Fournier v. Fournier*, 376 A.2d 100 (Me. 1977); *Rothman v. Rothman*, 65 N.J. 219, 320 A.2d 496 (1974).

In addition, it appears to be settled that the domiciliary state's property division provisions will generally affect all property of the spouses, even though originally created or acquired in another state. Clark, *Law of Domestic Relations*, Sec. 11.4 (1968); LeFlar, *Conflict of Laws: Dividing Property When Marriage Ends*, 1 Fairshare No. 8 at p. 9 (Aug. 1981). Certain residual problems continue to arise regarding real property outside the domiciliary state, but as a practical matter, those are usually settled by *in personam* jurisdiction of the dissolution court over the parties and its authority to decree certain actions by those persons before it in a litigated case. LeFlar, *op. cit.* at p. 10.

*The Act as a Property Statute:* Under the Act, property which a couple acquires from their respective efforts, as well as all income earned or accrued after the Act becomes applicable to that couple will be marital property. Each spouse will own an undivided one-half interest in that marital property. Consequently, in analyzing the property marshalled in a dissolution proceeding, each spouse is the owner of half of the marital property. If a state has provisions authorizing the alteration of property ownership by equitable distribution at divorce after the application of appropriate factors, then those factors and that authorized division would apply to marital property as it applies to the property each spouse owns prior to the adoption of the Act. Assume, as an example, that in a common law state without the Act spouses own all of their property as tenants in common, and that the state has an equitable distribution statute authorizing reallocation of property ownership in dissolution after the application of a set of factors. Also assume that after the application of the factors, a determination is reached that Spouse A should receive sixty percent of the total divisible property and Spouse B should receive forty percent. The dissolution court would have jurisdiction to reallocate ten percent of the property of one of the two tenants in common in favor of the other one in order to create the sixty-forty ratio of ownership.

If instead, all property of the couple was marital property under the Act, with everything else being identical, the same court could and should attain the same result. In both instances, property "owned" by one spouse is being reallocated in an equitable distribution proceeding to the other spouse. That is the precise way in which the ownership element in marital property should be applied and administered by a dissolution court under its equitable distribution statutes or procedures.

*Possible Adopting State Revisions:* Obviously an adopting state may wish to review its equitable distribution procedures and consider revising them after giving recognition to the effect of the adoption of the Act. However, the Act can and should function in a cognate fashion with respect to existing dissolution legislation. Coordination would certainly be necessary if an existing body of statutory law establishes a defined class of "marital property" to be marshalled and divided in the dissolution process only. That definition would have to be altered or omitted so that the definition of marital property in the Act would not conflict. However, not all states applying equitable distribution procedures follow a statutory definition of marital property. Some states apply their equitable distribution procedures to all property whenever and from wherever derived (Connecticut, Massachusetts). Some have judicial definitions of the universe of property to which their statutes apply (Florida, Ohio). Others have presumptions as to an appropriate division (Arkansas, North Carolina, Wisconsin). Still others have developed patterns of division which may have the same effect as a presumption (Pennsylvania). There are some fifty different systems in use, and virtually none of them is identical with any of the rest. See Freed, *Equitable Distribution as of December 1982*, 9 Fam. L. Rep. 4001 (1983) and Freed, *Family Law in the Fifty States: An Overview*, 4 Fam. L.Q. 289 (1983). Even if substantial statutory identity exists, case law has developed different answers to identical questions in different jurisdictions.

*Division in an Adopting State May Be Unequal or Equal:* It is not the mission of the Act to enter into the territory of equitable distribution or other systems of property division at dissolution. It is intended to operate as a property statute and to establish that a definite vested property interest exists in marital property from the instant of the creation of that property which traces through investment and reinvestment of the original property to property acquired with its proceeds. Consequently, a distribution different from an equal one in a dissolution of spouses owning marital property would simply be a property division dealing with the existing property rights of the spouses in marital property and reaching a particular result to achieve an equitable distribution of the marital property. Dealing with vested property rights in such a division is already a typical part of equitable distribution procedures. The Act is not designed to interfere with such a division under the statutes and cases in an adopting state or to ordain an equal division when that is not otherwise indicated.

What the Act will do is to create a different balance of ownership going in to the equitable division procedure from one which typically exists in common law jurisdictions in which title and ownership are synonymous.

**"Other Than Marital" Property At Dissolution:** What has been said relates to actual marital property, which is property acquired by efforts of a couple and from their income from all sources after the Act applies to them. Such a couple could be a couple married after the Act is adopted. It could be a couple living in an adopting state, both before and after the Act was adopted. It could also be a couple domiciled elsewhere and moving into an adopting state after the adoption. The "determination date" will be that event which renders the Act applicable to the property of each couple coming under its provisions. In the three situations, there will only be one in which the provisions of the Act would cover all post-marital income and all property acquired by productive efforts of the couple from and after their marriage so long as they live in the adopting state. That will be the couple marrying in an adopting state after the Act becomes effective and remaining in it until dissolution. As to couples in the other two situations, presumably they would have some accumulation of "other than marital" property which existed before the determination date and which could well have been marital property if the Act had been in effect when and where that property was acquired. That is obvious in the case of a couple marrying in and living in an adopting state both before and after the Act becomes effective. All of the income earned or accrued and the property acquired by productive efforts of that couple during their marriage would have been marital property if the Act had been in effect when it was acquired. Similarly, with a couple moving into an adopting state following adoption but bringing with them property which they had acquired in other jurisdictions, their income earned or accrued and property acquired by their productive efforts which was owned prior to moving into the state would have been marital property if in fact the Act had applied when and where it was acquired.

**The Deferred Approach:** The situation calls for an approach to deal with the property of couples who are seeking a divorce but who own something "other than marital" property. Section 17 applies a *deferred* marital property concept to that other property. An example will help to illustrate how it operates. Assume a couple always lived in an adopting state but lived there before the adoption. Before the adoption but during marriage, they acquired Blackacre with the proceeds of the employment of one or both of them. After adoption of the Act, they acquired Whiteacre with proceeds of employment occurring after the adoption. Their marriage is now dissolving. Whiteacre is clearly marital property and is owned in the equal undivided interests specified by the Act because it was acquired after the Act as the result of personal effort of one or both spouses and was marital property from its inception. On the other hand, Blackacre is some form of property other than marital property. That is because the Act does not operate retroactively, and Blackacre was owned before the Act applied to the couple. However, with the filing of the divorce suit, Blackacre is treated as if the Act had been in force when it was acquired, and will therefore be treated in the dissolution proceeding in a manner similar to Whiteacre.

**Comparison With Existing Approaches:** The way in which the section and the deferral concept operates is not substantially different from much existing equitable distribution legislation which provides that as of dissolution all of the property of the couple takes on the characteristics either of marital property or separate property (e.g., Colorado, Illinois, Missouri). That constitutes a deferred approach to such property, creating a class of dissolution-only marital property as of a deferred time namely the institution of the dissolution proceeding. A number of such statutes and procedures are in place in the several states, and the way this section operates is to follow the technique used in those statutes with respect to property which *would have been* marital property if the Act had been in effect as to the couple when and where the property was acquired. See Freed, *op. cit.*

**Certain Personal Injury Recoveries:** Subsection (b) deals with a matter related to Section 4(g)(6). The latter provision classifies as individual property a recovery for personal injury except for the component of the amount of the recovery attributable to expenses paid from marital property. Under Subsection (b) there is a deferred reclassification of any of that recovery that can be traced to the personal injury recovery as allocable to a loss of earning capacity. In the first instance, Section 4(g)(6) avoids the necessity of an allocation. That should make the personal injury action simpler. Ultimately, an allocation would be possible under Subsection (b) but only if there was still on hand at dissolution a traceable portion of the personal injury recovery allocable to a loss of earning capacity during marriage.

An example is illustrative. Assume a massive personal injury and a recovery of \$1,000,000. Assume no expenses were paid from marital property, so that the provisions of Section 4(g)(6) classified the entire amount as individual property. In a dissolution, some years later, the uninjured spouse is able to show that \$200,000 of the amount still on hand is fairly allocable to a loss of earning capacity. Then \$200,000 would be treated as if it were marital property, giving the uninjured spouse an opportunity to show that *before* the application of the



appropriate equitable distribution factors, \$100,000 could be treated as his or her marital property in the dissolution proceeding.

The rationale for the Subsection (b) treatment is that earnings are ordinarily marital property. By creating the possibility that residual amounts allocable to lost earnings could be marital property, an opportunity to achieve an equitable result in an appropriate case is presented. Loss of earning power is singled out because earnings would themselves have created marital property if they had not been lost. At dissolution it is appropriate to create some protection and replacement for the other spouse for the marital property that would have been there but for the injury. On the other hand, to have forced this determination at the time of the injury would impair the litigating posture, hence it is delayed to a point at which the issue significantly affects the interests of the uninjured spouse.

*Oversight Problems:* Subsection (c) is an "oversight" section. As pointed out in the Comments to Section 1(8), persons must be married to hold marital property. Ordinarily in a dissolution a disposition of all the property of the spouses will be made by decree or an agreement. Subsection (c) anticipates that this will occur, but makes a provision for a tenancy-in-common if satisfactory action has been omitted as to any former marital property. It is *not* a presumption or other indication that an equal division is either appropriate or required. Rather it deals only with oversight situations to clarify rights of former spouses when those rights have not been clarified by other documentation incident to the dissolution.

Subsection (d) is a bracketed section which would be appropriate in states in which a legal separation is recognized.

*Contractual Variance:* As with all provisions of the Act that contain no specific prohibition against contractual variance, the provisions of the section may be varied by a marital property agreement.

#### SECTION 18. TREATMENT OF CERTAIN PROPERTY AT DEATH OF SPOUSE.

(a) At the death of a spouse domiciled in this State, all property then owned by the spouse that was acquired during marriage and before the determination date which would have been marital property under this [Act] if acquired after the determination date must be treated as if it were marital property.

(b) At the death of a spouse domiciled in this State, any property of the spouse which can be traced to property received by the spouse after the determination date as a recovery for a loss of earning capacity during marriage must be treated as if it were marital property.

##### Comment

*The Deferred Approach At Death:* The deferred approach used in Section 17 at dissolution is also appropriate at death, and the reasons are substantially the same. A leading text explains the rationale:

"[T]here was almost universal acceptance of the rule that, when spouses changed their domicile, taking their property with them, the move did not change the classification of the property in the new domicile .... [I]f this move were from one state to another state having the same system of marital-property law, no serious problems arose. But when the move was from a common law state to a community property state, serious problems arose and inequitable results were the rule, not the exception. To hold that separate property from a common law state was also the husband's separate property in the community property state, and then to subject it to the laws of wills and succession of the community property state relating to separate property, changed its attributes and legal characteristics, and the rights and interests of the spouses in this property in a major way. What had happened in all these cases was that the wife had lost the protection furnished to her in the common law state by dower, or a statutory interest in lieu thereof, and had acquired no protection of any kind under the laws of the community property state.... It was noticed that, in most of the cases which reached the reviewing courts, nearly all of the property brought from the common law states was in the name of the husband and, under their law, was his separate property. When this was treated as the husband's separate property in the community property state, he could devise it by will to others than the spouse, and often did, the wife receiving no part of the estate." McClanahan, *Community Property Law in the United States*, Sec. 13.9 (1982).

California developed the initial response to the problem described by McClanahan and its solution appears in Cal. Prob. Code Sec. 201.5. Idaho has followed the California approach in Idaho Code Secs. 15-2-202 and 15-2-203. See also Reppy, *Community Property in California*, p. 292 ff (1980). Section 18 is similar to this legislation, although it does not use the same terminology. The approach is to create a *deferred* property right which applies at death. When it applies, property of the *deceased* spouse which would have been marital after

acquisition if it had been originally acquired under the Act is treated as if it had been so acquired for purposes of disposition at death. A provision regarding personal injury recoveries analogous to that in Section 17 is also included as Subsection (b).

*The Property Right:* There is an important parallel between the treatment of marital property at death and dissolution. It is that of the property right of the deceased spouse in the marital property as just that: a property right. The deceased spouse is the owner of a one-half undivided interest in marital property and it is subject to disposition at death as any other owned property. The ownership right is an integral part of the Act, expressly stated in Section 4(c). As with the same ownership right at divorce, it must be dealt with as an ownership right, and integrated into the probate system as property subject to disposition at death. If the spouse dies testate and the half interest in marital property is not disposed of by a non-testamentary method, it is subject to disposition as part of the testate estate. An attempt to dispose of more than the decedent's interest in marital property would be no different from an attempt to dispose of any other property a person did not own — it would be a nullity. It would amount to interference with the ownership right of the other spouse, subject to being dealt with as any such interference is already dealt with by applicable law.

*Appropriate Intestacy Provisions:* If a deceased spouse dies intestate, and an adopting state makes no change in its intestacy laws, the marital property interest of the decedent will be subject to intestate disposition. This raises interesting questions as to appropriate action in an adopting state. In the American community property states intestate disposition of separate property follows a pattern that varies from state to state as it does in common law states. All of the American community property states follow one pattern for disposing of community property and another for separate property. Obviously common law states have had no occasion for such a dual system and none is in place.

The typical intestate disposition of the first deceased spouse's interest in community property is in favor of the surviving spouse. However, that is not the universal rule. In California, Idaho, Nevada, New Mexico and Washington, upon the death of either spouse intestate, the decedent's half of the community property does pass to the surviving spouse. However, in Arizona, Louisiana and Texas, the decedent's half of the community property passes to the surviving spouse if there are no descendants. If there are descendants, the proportions vary from 100%, if all the surviving descendants are also descendants of the surviving spouse (Arizona), to one-half (Texas), to legal usufruct (life estate) only (Louisiana), to none, if one or more of the surviving descendants are not also descendants of the surviving spouse (Arizona).

*Uniform Probate Code Provisions:* There were significant historical reasons in the American community property states for bifurcating their intestate treatment of community and separate property which have never been present in American common law states. There would appear to be at least one element of community property intestacy law that ought to be followed by an appropriate alteration of intestacy laws by an American common law state adopting the Act. That would constitute following the recommendation set forth in Section 2.102A of the Uniform Probate Code. With respect to community property disposed of in intestacy, the recommendation was that "the one-half of community property which belongs to the decedent spouse passes to the [surviving spouse]." Apart from such an alteration, adopted to refer to marital property rather than community property, adopting states should require no substantial change in intestacy laws. Property other than marital property could remain subject to present patterns with the local preferences for particular schemes perpetuated. The logic of the alteration with respect to marital property is the logic at the heart of the Act, which is that of a sharing mode for marital acquisitions. A spouse who disapproves would have testamentary disposition as an option, and as noted below the testamentary disposition should not be subject to forced-share election.

*Forced or Elective Shares:* A corollary problem to intestate distribution is the elective share of a surviving spouse in testate dispositions. Among American community property states, only Louisiana's forced heirship provisions (in favor of others than the surviving spouse) interfere with the first deceased spouse's right of disposition of his or her share of the community. An adopting state should follow the majority rule and bar the enforcement of elective share rights of a surviving spouse against the interest in marital property of the first deceased spouse. The same reasoning would apply to the deferred marital property created by Section 18. The section itself establishes in the surviving spouse a half interest in the deferred marital property of the deceased spouse. Hence there is an effective statutory sharing in favor of the survivor in that property already established by the Act, and no further elective right in that property is needed or appropriate for that survivor. The result is that elective rights should be limited, if they are in fact perpetuated by an adopting state. They should apply only to individual property and other property in which the surviving spouse acquires no interest by the terms of the Act.

*The Novel Question For Adopting States:* With respect to elective share rights in an adopting state against property other than marital property or Section 18 deferred marital property, a substantial and novel question is presented. In community property states, separate property is not subject to elective rights by the other spouse. McClanahan, *op. cit.*, Sec. 11.4. The policy rationale is that community property rights are adequate protection and separate property is separate and should be under the unfettered control of its owner. However, if an adopting state followed that pattern it would represent a considerable retreat from existing spousal protection in most common law states. It would appear appropriate for an adopting state to retain elective rights against all property other than marital property and Section 18 deferred marital property, rather than to switch to the community property structure. However a major policy issue is presented by this question which each adopting state will necessarily consider for itself. A compromise might be the use of a lesser forced-share percentage against individual property than is presently in place. Here the issue of sharing will necessarily be considered in its fullest form, and the issues confronted will be *de novo*, since they have not previously been considered in this form in either common law or community property states. The closest approach was California's debate over quasi-community property which resulted in Cal. Prob. Code Sec. 201.5, previously discussed, but this did not present identical issues. In considering any possible revisions, an adopting state may wish to consider the data revealed and discussed in Fellows, Simon & Rau, *Public Attitudes About Distribution At Death and Intestate Succession Laws in the United States*, 1978 Am. B. Found. Research J. 319; see also Price, *The Transmission of Wealth at Death in a Community Property Jurisdiction*, 50 Wash. L. Rev. 277 (1975).

*Section 18 Protects the Survivor:* Section 18 is itself a statute that emphasizes protection to the survivor rather than the decedent. It does not treat all property of either spouse in the deferred mode, but only property acquired by the decedent. Thus the survivor will acquire a one-half interest in that property without the necessity of any election and without regard to will provisions. As with marital property, the surviving spouse will own a share of the deferred marital property as a property right and not as a result of exercising any elective right. Review of elective share provisions regarding this property is necessary. If appropriate in a state's statutory scheme, an attempt by a first decedent to defeat the operation of Section 18 should be barred by appropriate elective share provisions which would confirm Section 18 rights in favor of the surviving spouse. In Idaho the interest of a survivor in Idaho quasi-community property is protected by forced-share provisions. Idaho Code Secs. 15-2-202, 203. In California the quasi-community interest is simply stated as a property interest of the survivor. Cal. Prob. Code Sec. 201.5.

*The Administration Issue:* Historically the entire community was administered when a spouse died. See De Funiak and Vaughn, *Principles of Community Property*, Secs. 205-07 (1971). This pattern has been eroding. At this time, California and Nevada require administration only of the decedent's interest in the community. Arizona, Idaho, New Mexico and Washington follow the traditional pattern, though all four have simplified administration procedures under their versions of the *Uniform Probate Code* or Washington's non-intervention provision. Texas and Louisiana have simplified procedures when there is a surviving spouse but no issue, in Texas, or when succession without administration occurs, in Louisiana. In addition, Texas has independent administration as a possibility. See Mennell, *Community Property*, p. 355 ff (1982). An adopting state will necessarily face the administration issue and will be forced to consider whether the California and Nevada solution represents the appropriate trend.

The following sums up state intestacy, elective share and probate law provisions that would be appropriate for consideration by an adopting state for application on the death of a spouse subject to the Act:

(1) Type of Property Subject to Testamentary Disposition	(2) Amount Subject to Disposition By Decedent	(3) What Are Survivor's Rights of Election as To Amount In Column 2?	(4) Intestate Disposition As to Amount In Column 2
Marital Property	One-half	None (already owns other half of marital property)	To surviving spouse. If no surviving spouse (because of simulta- neous death) by existing law in adopting state
"Deferred Marital" or Section 18 Property	One-half	None, but should be given elec- tive right to secure survi- vor's half if necessary as in Idaho	Same
All other property subject to disposition at death by decedent	All	As provided by existing law in adopt- ing state	As provided by existing law in adopting state, includ- ing appropri- ate augmented estate provi- sions

As with all provisions of the Act that contain no specific prohibition against contractual variance, the provisions of the section may be varied by a marital property agreement.

**[SECTION 19. ESTATE BY THE ENTIRETIES.**

This [Act] does not affect the relationship between spouses and their creditors with respect to property held by spouses in an estate by entireties after the determination date.]

**Comment**

This is a bracketed section which would apply only in jurisdictions in which estates by the entireties are used.

The effect of the section would be to permit the continuation of the creditor protection afforded by the tenancy by the entirety provisions. See 41 Am. Jur. 2d *Husband & Wife* Sec. 55.

**SECTION 20. RULES OF CONSTRUCTION.**

Unless displaced by this [Act], the principles of law and equity supplement its provisions.

**SECTION 21. UNIFORMITY OF APPLICATION AND CONSTRUCTION.**

This [Act] shall be applied and construed to effectuate its general purpose to make uniform the law with respect to the subject of this [Act] among states enacting it.

**SECTION 22. SHORT TITLE.**

This [Act] may be cited as the "Uniform Marital Property Act."

**SECTION 23. SEVERABILITY.**

If any provision of this [Act] or its application to any person or circumstance is held invalid, the invalidity does not affect other provisions or applications of this [Act] which can be given effect without the invalid provision or application, and to this end the provisions of this [Act] are severable.

**SECTION 24. TIME OF TAKING EFFECT.**

This [Act] takes effect on January 1, 19[ \_\_\_\_ ].

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**SECTION 25. REPEAL.**

The following Acts and parts of Acts are repealed:

**Comment**

In an adopting state, it would be necessary to consider the interrelationship between provisions of the *Uniform Marital Property Act* and all other statutes of the state that affect the property rights of spouses. In particular, Section 15 would require attention to provisions concerning interspousal immunity from suits. Section 18 would require attention to intestacy and forced share provisions of probate laws.

**SECTION 26. LAWS NOT REPEALED.**

This [Act] does not repeal:

- (1)
- (2)
- (3)



# Appendix B

## Major Legislation Affecting Wisconsin Marital Property Act

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### Web sites for Legislation Affecting Wisconsin Marital Property Act

Revisor of Statutes Bureau

<http://www.legis.state.wi.us/rsb/stats.html>

1985 Wisconsin Act 37

<http://www.legis.state.wi.us/acts89-93/85Act37.pdf> (direct link)

1987 Wisconsin Act 393

<http://www.legis.state.wi.us/acts89-93/87Act393.pdf> (direct link)

1991 Wisconsin Act 224

<http://www.legis.state.wi.us/acts89-93/91Act224.pdf> (direct link)

1991 Wisconsin Act 301

<http://www.legis.state.wi.us/acts89-93/91Act301.pdf> (direct link)

1993 Wisconsin Act 160

<http://www.legis.state.wi.us/acts89-93/93Act160.pdf> (direct link)

1995 Wisconsin Act 27

<http://www.legis.state.wi.us/1995/data/acts/95Act27.pdf> (direct link)

1995 Wisconsin Act 201

<http://www.legis.state.wi.us/1995/data/acts/95Act201.pdf> (direct link)

1997 Wisconsin Act 188

<http://www.legis.state.wi.us/1997/data/acts/97Act188.pdf> (direct link)

1997 Wisconsin Act 250

<http://www.legis.state.wi.us/1997/data/acts/97Act250.pdf> (direct link)

1997 Wisconsin Act 297

<http://www.legis.state.wi.us/1997/data/acts/97Act297.pdf> (direct link)

2005 Wisconsin Act 216

<http://www.legis.state.wi.us/2005/data/acts/05Act216.pdf> (direct link)

2005 Wisconsin Act 443

<http://www.legis.state.wi.us/2005/data/acts/05Act443.pdf> (direct link)



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