

**Amendment to 08-02-03**

RESOLVED, that the Conference of Delegates of California Bar Associations recommends that legislation be sponsored to amend Family Code section 721 to read as follows:

- 1       §721  
2           (a) Subject to subdivision (b), either husband or wife may enter into any transaction with the  
3 other, or with any other person, respecting property, which either might if unmarried.  
4           (b) Except as provided in Sections 143, 144, and 146, ~~and 16040 and 16047~~ of the Probate  
5 Code, in transactions between themselves, a husband and wife are subject to the general rules  
6 governing fiduciary relationships which control the actions of persons occupying confidential  
7 relations with each other. This confidential relationship imposes a duty of the highest good faith  
8 and fair dealing on each spouse, and neither shall take any unfair advantage of the other. This  
9 confidential relationship is a fiduciary relationship subject to the same rights and duties of  
10 nonmarital business partners, as provided in Sections 16403, 16404, and 16503 of the Corporations  
11 Code, including, but not limited to, the following:  
12           (1) Providing each spouse access at all times to any books kept regarding a transaction for  
13 the purposes of inspection and copying.  
14           (2) Rendering upon request, true and full information of all things affecting any transaction  
15 which concerns the community property. Nothing in this section is intended to impose a duty for  
16 either spouse to keep detailed books and records of community property transactions.  
17           (3) Accounting to the spouse, and holding as a trustee, any benefit or profit derived from  
18 any transaction by one spouse without the consent of the other spouse which concerns the  
19 community property.  
20           (c) The “prudent investor rule” as set forth in Sections 16040 and 16047 of the Probate  
21 Code shall have no application in transactions between husband and wife.

(Proposed new language underlined; language to be deleted stricken.)

## RESOLUTION 8-02-2003

### DIGEST

#### Fiduciary Duty to Spouse: Prudent Investor Standard Inapplicable

Amends Family Code section 721 to confirm that the prudent investor standard does not govern financial decisions made by spouses.

### RESOLUTIONS COMMITTEE RECOMMENDATION

APPROVE IN PRINCIPLE WITH RECOMMENDED AMENDMENT

#### History:

Related to resolution 8-01-03.

#### Reasons:

This resolution amends Family Code section 721 to confirm that the prudent investor standard does not govern financial decisions made by spouses. This resolution should be approved in principle, with the recommended amendment, because it clarifies the duty of care one spouse owes to the other spouse with respect to financial issues.

Under the prudent investor standard, the investor is held to the level of knowledge and expertise possessed by a professional investment manager. Since *In Re Marriage of Duffy* (2001) 91 Cal.App.4th 923, and with the 2002 amendment to section 271, particularly the uncodified legislative intent language in Senate Bill No. 1936 (Stats. 2002, c. 310), there has been confusion in the family law field whether spouses are to be held to the prudent investor standard of care regarding financial dealings. In *Duffy*, the court held that there was no prudent investor standard between spouses. (*Duffy, supra*, at p. 940.) The 2002 amendment to the uncodified portion of section 721, apparently added to make clear that the statute agrees with the *Duffy* court holding, unfortunately states: “[i]t is the intent of the Legislature . . . to abrogate the ruling *In re Marriage of Duffy* (2001) 91 Cal.App.4<sup>th</sup> 923, to the extent that it is in conflict with this clarification.” As a result, some confusion has arisen over whether the Legislature rejected the *Duffy* holding.

This resolution makes the necessary clarification in the codified portion of section 721, stating the “prudent invest[or] rule” does not apply. Because clear statutory language prevails over uncodified “intent” language (see *People v. Statum* (2002) 28 Cal.4th 682, 689-690), this amendment should solve the problem. However, to avoid any possible future confusion, subdivision (c) of the resolution should be amended to change the words “prudent investment rule” to the “prudent investor rule,” which is the acknowledged term for this legal concept.

### SECTION/COMMITTEE REPORTS

#### FAMILY LAW SECTION

Recommendation: **APPROVE IN PRINCIPLE IF AMENDED**

#### Reason:

This resolution amends Family Codes section 721 by adding a paragraph (c) to clarify that the “prudent investor rule” does not apply to transactions between spouses, if amended to correct a “typo” from “prudent investment rule” to “prudent investor rule.”

### TRUSTS AND ESTATES SECTION EXECUTIVE COMMITTEE

Recommendation: **Approve in principle.**

**TEXT OF RESOLUTION**

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10 nonmarital business partners, as provided in Sections 16403, 16404, and 16503 of the Corporations  
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(Proposed new language underlined; language to be deleted stricken.)

PROPOSER: The Lawyers’ Club of San Francisco

STATEMENT OF REASONS

Existing Law: Uncodified Section 2 of Senate Bill 1936 (2002), Chapter 310, Statutes of 2002, amending Family Code section 721, states: “It is the intent of the Legislature in enacting this act to clarify that Section 721 of the Family Code provides that the fiduciary relationship between spouses includes all of the same rights and duties in the management of community property as the rights and duties of unmarried business partners managing partnership property, as provided in Sections 16403, 16404, and 16503 of the Corporations Code, and to abrogate the ruling in *In re Marriage of Duffy* (2001) 91 Cal.App.4th 923, to the extent that it is in conflict with this clarification.”

This Resolution: Clarifies that Family Code section 721 does not subject California spouses to the so-called “prudent investor standard” in their dealings with one another.

The Problem: The exceptions noted in subdivision (b) of Family Code section 721 relating to Probate Code sections 16040 and 16047 have been interpreted by the holding in *In re Marriage of Duffy* (2001) 91 Cal.App.4th 923, to mean that the “prudent investor rule” does not apply to transactions between husbands and wives. There is an argument that the language of the section could be interpreted as words of “inclusion” rather than “exclusion.” This has resulted in confusion in the meaning of the statute by

imprecise legislative intent language in SB 1936 itself, compounded by the legislative record of the bill. This resolution clarifies Section 721 to clearly reflect the non-applicability of the “prudent investor rule.”

The “prudent investor standard” essentially requires anyone subject to it to demonstrate the investment knowledge and expertise of a professional investment manager in all financial transactions. If the “prudent investor rule” were applied to transactions between husbands and wives, every financial transaction during a marriage—e.g., purchase or sale of a residence, investments in retirement plans, purchase or a sale of a business, or a deposit in a savings plan—could be scrutinized at the time of divorce. For example, if the “prudent investor rule” had been the law, at the end of the 1990’s spouses would have been suing each other for not investing in technology stocks. A few years later, the same spouses would have been suing each other for losing money in the same investment. Another commentator noted that any investment in a family farm would not meet the standard of the rule, and thus could be subject to litigation in a dissolution proceeding.

#### **IMPACT STATEMENT**

This resolution does not affect any other law, statute or rule.

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**RESPONSIBLE FLOOR DELEGATE:** LeRoy C. Humpal

#### **COUNTERARGUMENT**

##### **SAN DIEGO COUNTY BAR ASSOCIATION**

This resolution should be disapproved on the basis that spouses would no longer be subject to the prudent investment rule as set forth in Sections 16040 and 16047 of the Probate Code. Within the context of managing and investing trust assets, it is appropriate that parties, regardless of whether they are husband and wife, be held to the prudent investment rule standard. Spouses managing trust assets, should not be held to a lesser standard simply on the basis of their marital status.