Estate Planning Tools for Second Marriages

by David W. Kirch and Laurence I. Gendelman

This article explores estate planning for clients with previous marriages. It considers ethical issues and recent developments in the law relating to such planning and discusses tools to help clients achieve their goals.

Estate planning for clients who have previously been married presents unique challenges for practitioners concerning issues of both inheritance and family relations. This article advises estate planners on tools and best practices for working with clients who have previously been married.

Remarried couples face distinct estate planning issues. Most notably, spouses who bring children from a prior marriage into a new marriage typically want to ensure that these children inherit at least a portion of the assets brought into that new marriage. Additionally, couples who remarry are typically older and are more likely to each hold substantial separate property. Attorneys must be aware of these issues and be prepared to advise clients both verbally and in writing of the relevant legal considerations and options involving marital rights. The client's decision to choose, or to not pursue, particular options should also be committed to writing.

For the purposes of this article, "second marriage" refers to any subsequent marriage.

Ethical Considerations

Ethical issues in estate planning representation arise more frequently in second marriage situations, which are increasingly common due to the high rate of divorce and the fact that people are living longer.

Confidentiality

Client engagement letters should address confidentiality issues when planning is being done for both spouses in a second marriage.

Some experienced attorneys believe that separate representation of spouses is possible and that confidentiality exists as to each spouse. However, the ACTEC Commentaries on the Model Rules of Professional Conduct (MRPC) caution against this because a lawyer may be unable to adequately represent one spouse without disclosing a confidence of the other. ACTEC Commentary to MRPC 1.6 specifically provides that lawyers should exercise great care when representing both spouses because the lawyer has duties of impartiality and loyalty to each client and because separate representation of each spouse may limit the lawyer's ability to adequately advise each client.

Representation is not prohibited when a conflict of interest exists if the CRCP 1.7(b) requirements are met. Among other rule requirements, the client must give informed consent and waive the conflict in writing. Comment 22 addresses the effectiveness of such waivers, which is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails. As a practical matter, a letter evidencing the attorney's recognition of the conflict can be a double-edged sword, as recognition of the conflict may become relevant in a malpractice lawsuit.

Rights of the Surviving Spouse

It is always important to advise clients in second marriage situations of the surviving spouse's rights to the elective share and allowances and the presumption of joint tenancy as to tangible personal property.[1] Clients should be informed, in writing, that if their surviving spouse remarries, this creates a new set of rights in the new spouse, potentially entitling the new spouse to a large portion of the client's assets. Frequently, however, clients decide to simply trust each other.

Lawyers must also explain to clients that while they may have reached an informal agreement regarding their estate, the surviving spouse is not legally obligated to follow that plan. Experience indicates that more often than not, the relationships among the surviving spouse and the children of the deceased spouse deteriorate after the death of the first spouse. Therefore, clients should be advised in writing that absent a formal agreement, a surviving spouse has no

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obligation to maintain an estate plan that benefits the children of the deceased spouse.

In *Baker v. Wood, Ris & Hames, PC*,[2] siblings sued their father's attorney under the theory that the attorney owed them a professional duty. While the Court of Appeals found that the attorney did not owe any duty to the beneficiaries, estate planners should be cautious when working with clients who have children from previous marriages.[3] Documenting client decisions and confirming them in writing is a best practice to minimize lawsuits from dissatisfied beneficiaries of parents in second marriages.[4] If communication with a beneficiary becomes necessary, estate planners should provide that beneficiary with a written statement confirming their non-engagement and encouraging the beneficiary to seek independent legal counsel.[5] Otherwise, practitioners risk forming an attorney–client relationship with that beneficiary and having a professional duty to protect the beneficiary's interests.[6]

Estate Planning Tools

Useful estate planning tools for second marriage situations include trusts, contracts to will, gifts, life estates, divorce, and prenuptial and postnuptial agreements.

Trusts

Trusts are versatile tools that can add flexibility to an estate plan to deal with special issues that arise in a second marriage. If the client has children from a prior marriage, increased control over the disposition of the estate under the terms of a trust may be desired. For example, a trust may allow a surviving spouse to remain in the marital residence while also addressing what happens if that spouse no longer lives there, such as when the surviving spouse becomes institutionalized or acquires a new residence. The payment of expenses such as mortgages, taxes, repairs, and insurance on the residence should be addressed.

When no marital agreement exists, the surviving spouse could elect against the will of the decedent. Clients should thus consider including a forfeiture provision in the trust, such as: "In the event a statutory election is made, my surviving spouse shall be deemed to have predeceased me."[7] Otherwise, the value of the surviving spouse's interest in the trust will have to be determined in calculating the spouse's elective share or similar rights.

Clients must also consider that trust administration may add complexity and expense to estate administration.

Contracts to Will

"A contract to will is an agreement between two persons to devise property according to a 'common plan' by means of a contract that cannot be unilaterally revoked."[8] A contract to will becomes irrevocable and binding on the surviving spouse at the time of the first spouse's death. A contract to will may be written into the will itself or be made as part of a marital agreement or as a separate document (if the requirements for such documents to be binding are otherwise observed). A contract to will that is separate from the will may provide more flexibility and certainty than simply stating in the will that both spouses contract not to change their will. Frequently, prenuptial and postnuptial agreements and contracts to will are combined into one document or used in conjunction with one another to form an estate plan.

Contracts can be created through (1) provisions in the will stating the material provisions of the contract; (2) express reference to a contract in the will, and extrinsic evidence proving the contract terms; or (3) a decedent's signed writing evidencing a contract.[9] Mutual or mirror wills have sometimes been interpreted or found to operate as creating contracts to will.[10] To guard against such interpretation, language can be included in the will (or other planning document) stating that this is not the intent. This may be useful in some jurisdictions to counter a claim by the surviving spouse that a contract to will exists. In Colorado, no presumption of a contract to will is created by similar or mutual wills being executed simultaneously.[11]

A major advantage of using contracts to will is that the spouse who dies first has more control over the disposition of his property after the surviving spouse dies. Without a specific agreement already in place, the surviving spouse can typically change her will and how the property of the deceased spouse is treated.

Giving new life to the use of contracts to will, in *Murphy v. Glenn*[12] the Court of Appeals imposed a constructive trust on assets placed into a revocable trust contrary to the terms of a contract to will. Such an approach makes contractual wills more useful in states that recognize such equitable remedies, including Colorado. Otherwise, a claim against an estate for violation of a contract to will, where there are no probate assets, will be worthless.

Colorado follows the statutory trend of allowing additional categories of nonprobate assets to be recovered into the probate estate for access by creditors, giving contracts to will even greater utility.[13] Assets that are not subject to the statute include retire-

ment accounts, life insurance, and joint tenancy interests in real estate.[14] Colorado has added joint tenancy brokerage accounts to joint tenancy bank accounts as nonprobate assets that creditors can reach.[15]

Despite their usefulness, however, contracts to will are controversial and may encourage litigation or marital discord. It is also possible to circumvent a contract to will with nonprobate transfers.[16]

Clients must also consider tax consequences. Because contracts to will may be treated, for tax purposes, as a gift of the remainder interest in the surviving spouse's property to remaindermen, they may create an unexpected tax liability if the estate of the first spouse to die exceeds the current exemption amount. Thus, it is advisable to assume that property subject to a contract to will does not qualify for the marital deduction. Because the federal estate tax exemption has been substantially increased, however, this is less of a concern now for many clients.

Many contracts to will require both spouses to consent to future changes. This creates obvious problems if a spouse has a change of mind about the estate's disposition. Such modifications are more common the longer a marriage exists. There is also the possibility of undue influence by one spouse over another who has diminished capacity or is otherwise dependent on the spouse exerting influence.[17]

Contracts to will should be referenced in the parties' wills because with time such documents can easily be forgotten or misplaced.

Gifts to Children

Lifetime and testamentary gifts to children are also options to ensure that children by a prior marriage receive at least a portion of the estate if the parent is survived by a second spouse.

Lifetime gifts avoid the expense and burden of estate administration. And by not requiring children to wait until the death of the second spouse to receive their inheritance, lifetime gifts to children may also reduce resentment toward a second spouse.

Testamentary gifts include life insurance proceeds, which may be particularly appealing because (1) they are new wealth arising at death, so the surviving spouse may be less inclined to feel deprived of a marital asset, and (2) they pass outside of probate. IRAs are another potential asset to use as a gift to children because the tax treatment of distributions from IRAs makes them less available during the life of the participant.

Life Estates

A life estate is another estate planning tool often used to ensure that a portion of the parent's estate goes to the children of a prior marriage. To create a life estate, a spouse who owns property provides that upon that spouse's death the surviving spouse receives a life estate with a remainder interest to the deceased spouse's children. This arrangement allows the surviving spouse to live in the house without having the power to alter who subsequently receives the property.

When creating a life estate, attorneys should designate who will be responsible for the payment of mortgages, real estate taxes, insurance, maintenance, and improvement expenses to minimize uncertainty and conflict between the deceased spouse's children and the second spouse.

Unlike a trust, this arrangement cannot be used to address the possibilities that (1) the surviving spouse may want to move from the residence, (2) the residence may be sold and a replacement residence may be desired, and (3) the surviving spouse may remarry.

Clients must also consider that life estates gifted during the life of a decedent will not qualify for the gift tax marital deduction because they are not a qualified terminable interest.[18]

Divorces to Create Medicaid Eligibility

In Colorado, spouses can be held liable for each other's medical bills.[19] Frequently, spouses in second marriages are unaware of their potential liability for the new spouse's medical expenses. This is of particular concern for the spouse with greater assets.

Medicaid is a federally funded program that pays medical expenses for low-income elderly and disabled persons. Because Medicaid is the primary governmental program paying for long-term nursing home care, it is an attractive option for the elderly. Participation by state in Medicaid is voluntary, and laws vary by state. Federal law mandates certain eligibility and service standards,

and if a state participates, state and federal funding combine to pay for Medicaid medical expenses.

With their combined income and assets, many married couples do not qualify for Medicaid coverage. But for some couples, divorce may allow the more impoverished spouse to qualify for Medicaid. For marriages in which only one spouse seeks Medicaid coverage and the other has substantial assets, divorce may preserve marital assets while also helping a spouse to qualify for coverage. From an economic standpoint, the advantages of divorce may outweigh its costs.

But there may be obstacles to obtaining a divorce for the purpose of securing Medicaid eligibility (e.g., a client's religious or personal values opposing divorce), and a court may determine that a spouse with diminished capacity lacks the requisite state of mind to consent to a divorce (but a Colorado statute specifically allows a conservator to file a divorce action on behalf of a protected person).[20]

Of course, encouraging a couple to get divorced is arguably against public policy, and disadvantages of divorcing to secure Medicaid eligibility must be considered. These include the emotional toll on the couple and their families, and that divorced spouses will not qualify for certain federal safety nets designed to protect aging spouses.[21] Divorce may also result in more complicated and contentious estate administrations; a property division favorable to the propertied spouse may be viewed as a disqualifying gift. Moreover, divorce often requires spouses to redraft estate planning documents.

Prenuptial and Postnuptial Agreements

Currently, only Colorado and North Dakota have adopted the Uniform Premarital and Marital Agreements Act (UPMAA). Colorado enacted the UPMAA in 2013 effective July 1, 2014. The UPMAA "chooses to treat prenuptial agreements and postnuptial agreements under the same set of principles and requirements."[22] Because governing law can vary greatly from state to state, such agreements should (1) specify which state's law will govern and (2) allow for amendment of the agreement if parties move to another state, because some states do not allow for postnuptial agreements. There are several statutory requirements concerning prenuptial and postnuptial agreements that practitioners should consider when drafting, enforcing, and challenging these agreements.[23]

The major advantage of prenuptial and postnuptial agreements is that they avoid the uncertainty of judicial interpretation and differences in state law. They also prevent one spouse from unilaterally changing the terms of the agreement because spouses must consent to all material changes. Such agreements also override default rules that apply when a person remarries. Finally, prenuptial and postnuptial agreements make the intentions of the parties clear, thereby reducing chances of later disputes.

The potential of divorce must be considered when drafting these agreements. The surviving spouse receives myriad rights upon the first spouse's death, but spouses can waive these rights, either in whole or in part, in a prenuptial or postnuptial agreement. By waiving all rights in a prenuptial or postnuptial agreement, the surviving spouse gives up the right to the elective or spousal share, the family allowance, and the exempt property allowance, as well as priority to serve as personal representative.

To be enforceable under the UPMAA, the waiver of rights upon death must be contained in a valid prenuptial or postnuptial agreement that is signed by both parties, specifically identifying the rights waived.[24] When drafting such an agreement, it is important to be as specific as possible as to which rights are to be waived. The Court of Appeals in *In re Estate of Smith*,[25] which dealt with spousal rights at death, held that a statement that the spouse agreed with the decedent's will did not constitute a specific enough waiver of "all rights" in the event of death to be effective under the statute. *Smith* reflects the strong public policy frequently recognized by the courts in favor of protecting marital rights. Similarly, in *In re Marriage of Stokes*,[26] a spouse's waiver of "future acquisitions" was sufficient to bar access to future appreciation of separate property, but was insufficient to bar a claim for spousal maintenance.

When drafting a prenuptial or postnuptial agreement, issues regarding retirement benefits and interests in nonmarital trust assets should be addressed.

Retirement benefits. "A participant in a retirement plan cannot obtain a valid waiver of spousal survivorship rights prior to the parties' marriage. Thus, [in prenuptial and postnuptial agreements,] the general waivers of 'all rights upon death' or even a specific waiver of rights to a retirement plan, will not constitute an effective waiver of spousal survivorship rights in a retirement plan."[27] Despite such invalidity, many prenuptial agreements still include retirement plan waivers. To ensure enforceability, these waivers should be accompanied by mutual promises to execute separate retirement plan waivers once the parties marry.

In *Egelhoff v. Egelhoff ex rel. Breiner*,[28] the U.S. Supreme Court held that revocation-on-divorce statutes are inapplicable to the extent that the beneficiary designation is associated with an ERISA-governed account or retirement plan, and that ERISA-governed account proceeds remain payable to the named ex-spouse. Federal preemption would also invalidate the provisions of a prenuptial agreement that contained a waiver of rights in ERISA plans, if a proper post-marriage waiver were not executed.

However, recent case law and commentary suggest that, under an unjust enrichment theory, a constructive trust may be imposed on ERISA-governed account proceeds once they have been distributed to the spouse.[29] Such reasoning supports a constructive

trust remedy when a post-marriage waiver was not executed under the terms of a prenuptial agreement. In any event, clients should be advised to obtain the necessary waivers to ERISA benefits as soon after the marriage as possible.

Interests in nonmarital trust assets. Trusts existing at the time of marriage or created during marriage by third parties are initially separate property. However, in Colorado, income from, and appreciation to, separate property is considered marital property.[30] It may be advisable to specifically include a waiver of rights to the income and appreciation on separate property and to interests in trusts. Courts conduct a two-part analysis in making property divisions in divorce proceedings: (1) Does the interest in the trust constitute "property" within the meaning of the statute? And if so, (2) is the interest separate property or marital property?

Colorado statutes limit treatment of third-party revocable trusts as property. In 2002, responding to a case in which a revocable trust was treated as property, Colorado revised its dissolution of marriage statute to provide that

> "property" and "an asset of a spouse" shall not include any interest a party may have as an heir at law of a living person or any interest under any donative third party instrument which is amendable or revocable, including but not limited to third-party wills, revocable trusts, life insurance, and retirement benefit instruments, nor shall any such interests be considered as an economic circumstance or other factor.[31]

In *In re Marriage of Balanson*,[32] a wife's remainder interest in an irrevocable trust was found to be property, despite her father's income interest and the right to invade the principal (i.e., subject to complete defeasance). "These factors render the value of wife's remainder interest uncertain, but do not convert her interest into a mere expectancy."[33] The Colorado Supreme Court deemed the wife's remainder interest a "future vested interest" rather than a mere expectancy.[34] On the other hand, in *In re Marriage of Guinn*,[35] a spouse's future income interest in an irrevocable trust was not "property" for dissolution of marriage purposes. "[W]hen the beneficiary has no interest in the corpus, and no right to control how the corpus is invested . . . the income is a mere gratuity deriving from the beneficence of the settlors."[36]

Conclusion

Ethical issues frequently arise when estate planning with spouses in a second marriage, but these can often be addressed with informed, written consent. It is important to advise clients of spousal rights that could impact their estate planning. A variety of tools, including trusts, contracts to will, gifts, life estates, divorce, and prenuptial and postnuptial agreements are at the estate planner's disposal to protect remarried spouses and their beneficiaries, including children from a prior marriage.

Notes

1. *See* CRS §§ 15-11-201 et seq. (elective share); CRS §§ 15-11-401 et seq. (allowances); CRS § 15-11-805 (joint tenancy).
2. *Baker v. Wood, Ris & Hames, PC*, 364 P.3d 872 (Colo. 2016).
3. *See* Millard, "Estate Planning and Administration in Colorado after *Baker v. Wood, Ris & Hames, PC*," 45 *The Colorado Lawyer* 43 (Oct. 2016).
4. See *id*.
5. *Id*.
6. *Id*.
7. Fleisher, "The Contract to Will—A Proposed Solution," 29 *Colorado Lawyer* 49, 50 (Apr. 2000).
8. Johns et al., "Joint Trusts As a Contract to Will," *The Colorado Estate Planning Handbook* § 15.6.4 (CLE in Colo., Inc., 6th ed.).
9. CRS § 15-11-514.
10. *See Trindle v. Zimmerman*, 172 P.2d 676 (Colo. 1946).
11. CRS § 15-11-514.
12. *Murphy v. Glenn*, 964 P.2d 581 (Colo.App. 1998).
13. *See* CRS § 15-15-103.
14. CRS § 15-15-103(1)(b).
15. *Id.*
16. *But see Murphy*, 964 P.2d at 581, which would permit reaching nonprobate transfers determined not to have been made in good faith.
17. *See Krueger v. Ary*, 205 P.3d 1150 (Colo. 2009).
18. IRC § 2523(f).
19. *See* CRS § 14-6-110.
20. CRS § 15-14-425.5. *See also* Farley, "When 'I Do' Becomes 'I Don't': Eliminating the Divorce Loophole to Medicaid Eligibility," 9 *Elder L.J.* 27, 41 (2001).
21. *See* Social Security Act, 42 USC §§ 1396r-5 (community spouse minimum monthly maintenance needs allowance and resource allowance).
22. *See* Unif. Marital and Premarital Agreement Act (2012).
23. *See* CRS §§ 14-2-301 et seq.
24. Boothby and Willoughby, "Colorado's New Uniform Premarital and Marital Agreements Act," 43 *The Colorado Lawyer* 57 (Mar. 2014).
25. *In re Estate of Smith*, 674 P.2d 972 (Colo.App. 1983), *modified* 718 P.2d 1069.
26. *In re Marriage of Stokes*, 608 P.2d 824 (Colo.App. 1979).
27. Alexander and Sullivan, "Marital Agreements and Estate Planning, Denver Estate Planning Council" at 17 (Mar. 17, 2011).
28. *Egelhoff v. Egelhoff ex rel. Breiner*, 532 U.S. 141, 148 (U.S. 2001).
29. Kesselman, "Can State Law Remedies Revive Statutes Stricken by ERISA's Preemption Provision?" 38 *ACTEC L.J.* 245, 251 (2012).
30. *See In re Marriage of Foottit*, 903 P.2d 1209 (Colo.App. 1995), where a trust's income produced during the marriage was found to be marital property.
31. CRS § 14-10-113(7)(b) (responding to and superseding *In re Marriage of Gorman*, 36 P.3d 211 (Colo.App. 2001)).
32. *In re Marriage of Balanson*, 25 P.3d 28 (Colo. 2001).
33. *Id.* at 41.
34. *Id*.
35. *In re Marriage of Guinn*, 93 P.3d 568 (Colo.App. 2004).
36. Chorney, "The Continuing Evolution of Balanson: Trusts as Property in Divorce," 34 *The Colorado Lawyer* 89, 93 (June 2005) (citing *Guinn*). ■