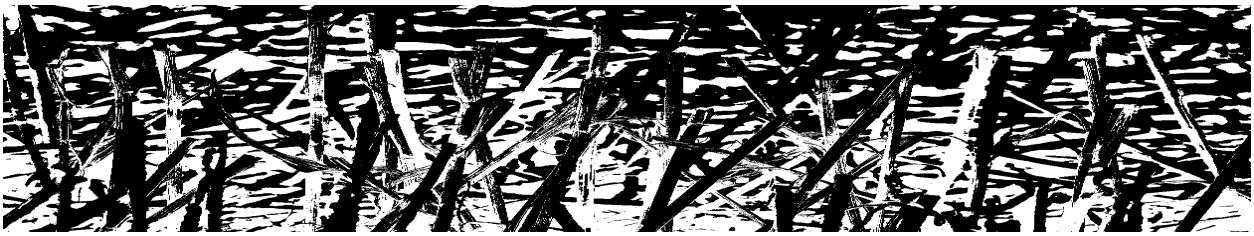

Jack Straw Fortnightly*

Gang aft agley

Until last Thursday, it had been my plan to commit much of this issue to a discussion of the June 11 Supreme Court decision in *Sveen v. Melin*. But something came up.

Deconstruction

Justice Kagan, writing for an eight-member majority, rejected the argument that "retroactive" application of a Minnesota statute which treats divorce as revoking nonprobate beneficiary designations for a former spouse would violate the "contracts clause" of the federal constitution.

The word "retroactive" as used here does not mean the statute was enacted after the couple was already divorced. The statute in its present form was enacted in 2002,[fn. 1] and the divorce occurred in 2007. But the insurance policy had been purchased in 1998.[fn. 2]

The insured died in 2011,[fn. 3] without having changed the beneficiary designation. Both the former spouse and the decedent's two children, as designated alternate beneficiaries, claimed the proceeds, and the insurer, MetLife, interpleaded.

The trial court granted summary judgment to the kids, and the former spouse appealed. The 8th Circuit federal appeals court reversed, citing its own 1991 decision in *Whirlpool Corp. v. Ritter*, in which it had ruled a similar Oklahoma statute improperly "impaired the obligation" of a life insurance contract, to pay the proceeds to the named primary beneficiary.

If I had written this up, I might have begun with Justice Gorsuch's remarkably facile dissenting opinion. The "obligation" of the insurance contract, he says, is to pay the proceeds to the designated beneficiary, here the former spouse. The statute "impairs" that obligation, QED.

The majority goes wrong, he says, first by construing the contracts clause in a weakened form, which permits a state to enact legislation that "substantially" impairs a contractual obligation, provided the legislation serves a "significant and legitimate" public purpose and the impairment is "reasonable" and "appropriate" to that purpose, and then by finding the impairment here to be insubstantial.

The items called out in quotes are from the Court's 1983 decision in *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, which Justice Gorsuch seems to identify as an unfortunate turning point in the Court's interpretation of the contracts clause. Back in the day, about 1819 or thereabouts, the prohibition against state legislation retroactively impairing contracts was understood to be absolute.[fn. 4]

The majority, as noted, determined that the impairment here was not "substantial," so that it was not necessary to reach the questions whether the legislation served a "significant and legitimate" public purpose, etc.

Their argument, as articulated by Justice Kagan, was (a) in the typical case, the statute would further the policyholder's intent, rather than impair it, (b) the result the statute effects is what the policyholder would likely have expected in the event of a divorce anyway, and (c) the policyholder can easily override the statutory presumption by redesignating the former spouse as beneficiary, after the divorce.

If someone tells her she has to.

This analysis largely tracks an amicus brief filed by ACTEC, which quoted at length from a 1991 statement of the "joint editorial board" for the Uniform Probate Code, decrying the *Ritter* decision as "manifestly wrong" because (a) the insurer's obligation to pay someone, whoever, was not impaired, (b) the "default" rule expressed by section 2-804 serves "to implement rather than to defeat the insured's expectation" under the contract, and (c) there was no prior caselaw applying the contracts clause to changes in statutory rules of construction.[fn. 5]

That joint statement somewhat mischaracterized section 2-804 as providing a "default" rule of construction, revoking a beneficiary designation in favor of the former spouse "unless the policy owner expresses a contrary intention."

In fact the only way the policyholder holder can override the statutory presumption is by redesignating the former spouse after the divorce.

If I had written this up, I also would have highlighted a fascinating amicus brief submitted by the Women's Law Project, together with more than a dozen other organizations promoting gender equality, persuasively arguing that revocation on divorce statutes disproportionately injure women, and that retroactive application of these statutes is "neither reasonable nor appropriately tailored to their purported public purpose."[fn. 6]

Again, the majority did not reach these questions because they found no "substantial" impairment of the insurance contract in the first instance.

But ultimately I would have tried to develop an argument that the entire contracts clause discussion misses the mark.

What actually is the contract here? MetLife promises to pay the proceeds to whoever the policyholder has designated. The policyholder reserves the right to revoke any designation. [fn. 7] The statute construes divorce

as revoking a designation in favor of the former spouse.

The presumption is effectively irrebuttable, and while this may not be good policy, it does not implicate the contracts clause, at all.

The former spouse might still have a remedy if -- as in fact was alleged in this case -- she had an enforceable agreement with the policyholder to keep the beneficiary designation in place.[fn. 8] The revocation on divorce statute does not purport to impair such an agreement.

But as I say, something came up.

Errata

Oh, and another matter I had intended to address in this issue.

Some readers will recall that in Jack Straw number six I was carrying on about the new ACGA recommended gift annuity rates, which went into effect on July 1. About how a half point increase in the assumed rate of return on investment might be overly optimistic, etc.

In the course of that screed, I referenced an analysis Bill Laskin had posted to the PGCalc blog, and in my paraphrase I attributed to him an inference he did not actually draw, *viz.*, that

> the new recommended rates will fail the twenty pct. requirement for some younger annuitants if the section 7520 drops below 2.8 pct., and will fail the ten pct. requirement if the rate drops below 1.8 pct.

Bill e-mailed me to thank me for the shout out, but gently pointed out that his analysis dealt only with the ten pct. requirement. For those of you playing at home, what I am calling "the twenty pct. requirement" is something the ACGA instituted in January 2012 as a stabilizer after they had had to change the recommended rates five times in three years when interest rates fell to near zero.

On the face of it, it seemed to me that the one implied the other, and Bill and I had a friendly exchange of e-mails over a couple or three days trying to sort it out.

He put in a call to David Ely, who chairs the rates committee, and confirmed something I might have figured out if I had thought about it more carefully.

The twenty pct. threshold is calculated using a different methodology, and actually has nothing to do with the section 7520 rates.

Specifically, quoting here from one of Bill's e-mails -- having maybe learned the hazards of paraphrasing --

> the twenty pct. present value requirement is computed by the actuaries who developed the suggested maximum rates on behalf of the ACGA. They use the same interest rate and 2012 IAR mortality table for all their calculations. The monthly AFR is irrelevant for purposes of the twenty pct. present value calculation.

My takeaway is that the recommended rates are probably structured to meet

the twenty pct. threshold in any circumstance in which the annuity would meet the ten pct. requirement -- or more to the point, in any circumstance, period, because the rate of return assumptions are fixed.

Counting coup

But all of that was pre-empted by a voicemail I received last Thursday from the office of my state senator, Olivia Cajero Bedford.

Two years ago, I had written her, and my two state representatives, to ask whether one or another of them might ask the state attorney general for a formal opinion on whether either or both of two amendments to section 14-2901 of the Arizona statutes might violate the state constitutional prohibition against legislation "permitting any perpetuity or entailment in this state."

Historically, and in light of this provision in the state constitution, Arizona courts had followed the common law rule, which says that a nonvested future interest in property is not valid unless it is certain to vest or fail within twenty-one years after the death of some person who is alive at the time the interest is created.

Already I can see your eyes glazing over.

But I will have you know that this -- what we are talking about right here, the "race to the bottom" among state legislatures, acting at the behest of bankers and lawyers, to try to attract and keep trust administration business in state by relaxing traditional rules that have protected against abuse of the form of property ownership known as the "trust" -- this is the entire focus of what I have been calling "the Greystocke Project."[fn. 9]

I sort of stumbled into this fixation after I unexpectedly found myself on the receiving end of some rather astonishing abuse on a listserv because I happened to disagree with someone's reading of a state supreme court decision.

At issue in the listserv thread -- but not in the court's decision, which is the point I was making -- was the validity of a state statute extending a "wait and see" statute to several hundred years, in the face of a state constitutional provision forbidding perpetuities.

About nineteen messages in to an increasingly heated exchange, my antagonist characterized my reading of the decision as "libelous." That caught my attention. The only possible meaning of that adjective in context would be trade libel. We are trying to build a trust haven here, and we need you to shut up about what this decision does or does not mean.

Almost immediately, I set about writing a three thousand word article questioning the viability of the 2010 decision of the North Carolina appeals court in *Brown Bros. Harriman Trust Co. v. Benson* as precedent on the question whether a statute abrogating the rule against perpetuities as to trusts violated that state's constitutional prohibition of "perpetuities."

Perhaps not surprisingly, I encountered some difficulty getting that article published.

Anyway. To the subject at hand.

The common law rule is actually referenced in section 33-261 of the Arizona statutes, which is still on the books, but was superseded as to interests created on or after December 31, 1994 by the enactment of a version of the uniform statutory rule against perpetuities.

The statutory rule substitutes a ninety-year "wait and see" mechanism for the common law rule that would otherwise invalidate a future interest that might fail under any scenario on day one.

But in 1998, section 14-2901 was amended to abrogate the common law rule against perpetuities altogether if the future interest is in a trust and the trustee has a power of sale -- provided that someone who was alive when the trust was created has a power, exerciseable at some point after the trust was created, to terminate the interest.

And then in 2008, the "wait and see" period was extended to five hundred years -- somewhat longer than the rule itself has been a feature of the common law.

My letter two years ago was, how you say, a "polemic." But to her credit, in making the request for a formal opinion, Sen. Cajero Bedford simply asked the question, without any framing arguments. And this may have contributed to the favorable outcome.

Oh, did I mention.

The voicemail I received last Thursday was to tell me the state attorney general had issued an opinion saying each of these two amendments to the Arizona statute is "likely unconstitutional."

Just one victory, as Todd would say. The next step is to try to persuade these legislators to get behind a bill to repeal these two amendments.

But first, maybe I should register with the state as a lobbyist on behalf of the Project.

What good are notebooks

[fn. 1]

The statute largely tracks section 2-804 of the 1990 revision to the Uniform Probate Code, and as the majority opinion noted, "substantially similar" statutes have been enacted in slightly more than half the states.

The predecessor to this section of the Minnesota statutes, and of the uniform code, applied only to provisions for a divorced spouse under a decedent's will.

[fn. 2]

You want to see a case in which a "revocation on divorce" statute was applied retroactively to a divorce that preceded its enactment, take a look at *Stillman v. TIAA-CREF*, a 2003 decision out of the 10th Circuit.

No cert petition there.

[fn. 3]

From the trial court decision we learn that this was a suicide. And we also learn that the amount in controversy was -- wait for it -- $180k.

Nonetheless, both sides lawyered up for the cert petition, Jenner & Block for the petitioners, Jones Day for the respondent. The question is, who was paying these guys.

[fn. 4]

A much fuller discussion of the Court's history with the contracts clause is given in an amicus brief authored by James W. Ely, Jr., professor emeritus of both law and history at Vanderbilt. Prof. Ely argued that the wrong turn was taken in 1934, with the decision in *Home Building & Loan Association v. Blaisdell*.

Jack finds this entire discussion fascinating, but he accepts that it is beyond the immediate scope of this newsletter.

It is interesting to note that none of the other "originalists" on the bench joined the dissent or wrote separate opinions concurring in the result only.

[fn. 5]

The ACTEC brief also argued that the appeals court had been "paralyzed" by its own prior decision in *Ritter*, and "unable to benefit from primary and secondary authorities that post-dated [that] decision," much as it might have wanted to.

A fair reading of the appeals court's decision does not in the least support this inference.

[fn. 6]

The same coalition had also filed an amicus brief supporting the cert petition in *Lazar v. Kroncke*, an essentially identical case, albeit involving a the designation of a former spouse as beneficiary of a decedent's IRA. The petition in *Lazar* was denied a week after the decision in *Sveen*.

[fn. 7]

It bears noting that until not quite a hundred years ago, equity courts treated the designated beneficiary's rights under an insurance contract as vested, absent language in the contract expressly reserving to the policyholder a power to revoke.

An excellent article on the development of the law relating to rights of third party beneficiaries, authored by an assistant editor, appeared in a 1982 issue of the Cornell Law Review.

[fn. 8]

Provided the agreement was in writing or had been entirely performed on one side. Unfortunately, neither was the case here.

If in fact there was an agreement, it would have been advisable to incorporate that into the divorce decree. Ms. Melin may yet have a remedy against her divorce lawyer for malpractice. Assuming the statute has not run.

[fn. 9]

The name "Greystocke" is an admittedly obscure reference to the barony that was at issue in the so-called Duke of Norfolk's Case, decided in 1682, which is credited with having first laid the groundwork for what ultimately became the common law rule against perpetuities.

Jack says, you need your head.