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Premarital and Postmarital Agreements in Minnesota

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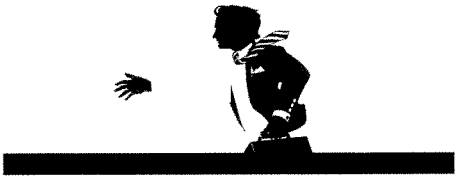

LAWYER AT LARGE

PREMARITAL AND POSTMARITAL AGREEMENTS

BY WILLIAM E. MULLIN AND JUDITH T. YOUNGER

Premarital agreements — agreements between prospective spouses made in contemplation and consideration of marriage — and postnuptial agreements — agreements between spouses made after and during marriage — share a number of common characteristics which distinguish them from other contracts. These common characteristics have led some jurisdictions to adopt identical standards for testing the validity of premarital and postnuptial agreements.[1] Unfortunately, this is not the case in Minnesota. Recent legislation prescribing special requirements for postmarital agreements prevents all but the wealthiest couples from using these agreements and introduces additional complications which restrict their use.

ALIKE, BUT DIFFERENT

Premarital agreements appeared in modern form in 16th century England. Both chancery and common law courts were passing on their validity.[1] Parties used them to evade the common law rules depriving wives of the legal capacity to own property and make contracts.[2] Those very rules made postmarital agreements useless.

Husbands and wives were considered one legal person, *i.e.*,, the husband, so wives could not contract with their husbands or anyone else.[3] In the 19th century, the Married Women's Property Acts restored wives' legal capacity to make contracts and own property.[4] Postmarital agreements then became viable tools for embodying contractual understandings between spouses.

Despite their different histories, the two kinds of agreement have three common characteristics which distinguish them from other contracts. First, the parties are in confidential relationships; this increases the possibility that one party might overreach the other. Second, the subject of these agreements is usually family finances; couples use them to govern their property and support rights. Thus, these agreements are of greater interest to the state than ordinary commercial contracts. Third, there is often a long period of time between execution and enforcement of these agreements; this increases the possibility that unforeseen events may make it unwise or unfair to enforce them.

"The ideal state of law would be for the well-understood requirements for premarital agreements to apply to postmarital agreements as well."

PREMARITALS IN MINNESOTA

Prospective spouses in Minnesota can now use premarital agreements to govern their rights in both marital and nonmarital property. The Minnesota Legislature and the Minnesota Supreme Court have set down standards for testing their validity.[6] At execution, premarital agreements must be procedurally and substantively fair; at enforcement, they must be substantively fair.[7]

The procedural fairness required at execution is described in M.S.A. section 519.11. The agreement must be executed before the day on which the marriage is solemnized. Each party must have had the opportunity to have an attorney of the party's choice. Each must make full and fair disclosure of earnings and property, and certain formalities must be met. Premarital agreements must be in writing and they must be acknowledged and executed in the presence of two witnesses. Agreements dealing with realty must be recorded in the same manner as deeds. The requirement of substantive fairness, at execution and enforcement, emanates from common law and is assessed by the courts on a case-by-case basis.[8]

ENSURING FAIRNESS

Lawyers and clients can ensure the procedural and substantive fairness of premarital agreements at the time of execution. Section 519.11 provides only that each party must have had an opportunity to have separate counsel of choice and the Minnesota Supreme Court has held that the fact that one lawyer represents both parties does not in itself make the agreement procedurally unfair at execution.[9] Nonetheless, the lawyer representing a party to such an agreement is well-advised to insist that the other party be separately represented. This avoids litigation, fairly common in our state, over whether a spouse's opportunity for separate counsel was real or sham.[10]

Counsel should make sure that the parties make full financial disclosure before the agreement is executed. Accurate schedules of the parties' assets should be incorporated into the agreement itself. Counsel should urge the parties to eliminate provisions likely to be attacked later as unfair. An arguably unfair provision should be accompanied by recitals of the circumstances justifying it. Such recitals might satisfy a court if litigation ensues when a party seeks to enforce the provision.

It is harder, of course, to prepare for judicial review of substantive fairness at enforcement, perhaps years later. Neither clients nor lawyers can control the future. The birth of a child or changes in the financial status, employment, or health of a party may make an agreement that was procedurally and substantively fair at execution, unfair at enforcement. To reduce the chance of such a result, the lawyer should attempt to foresee possible future events and provide for them. Future events which the parties knowingly provide for do not trouble the courts as much as unforeseen events about which the agreement is silent.

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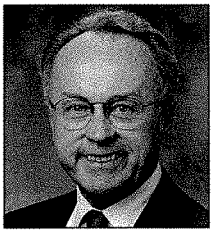

POSTMARITALS IN MINNESOTA

Until recently, Minnesota law on postmarital agreements, while less developed than that on premarital agreements, has been workable for the practicing lawyer. M.S.A. section 519.06 unequivocally permits husbands and wives to contract with each other on any subject.[11] But a single Minnesota Court of Appeals opinion, *Lerner v. Lerner*,[12] unaccountably holds that, for a postmarital agreement to be valid, the spouses must be living apart at execution. With an eye on this case, good lawyers have been drafting postmarital agreements for their clients, whether the clients are living together or apart, warning that they might not hold up. While the established standards for testing the validity of premarital agreements did not explicitly apply to postmarital agreements, most lawyers tried to comply with them anyway, knowing that courts would treat an agreement more kindly if procedural and substantive fairness attended its execution.

NEW REQUIREMENTS

The law changed on August 1, 1994. In response to what appears to be private lobbying on behalf of a wealthy couple, the Minnesota Legislature amended section 519.11 to add new provisions governing postmarital agreements. They override[13] section 519.06 and the *Lerner* case, and explicitly provide that, to be enforceable, postmarital agreements must comply with the requirements for premarital agreements. The Legislature went on to prescribe additional requirements for postmarital agreements only.

FIRST, each spouse must, at the time of execution, actually be represented by separate counsel. The legislation leaves the present requirement for premarital agreements — that each party need only have had the opportunity to be represented by counsel of choice — intact. This draws an unwarranted distinction between the two types of agreement but poses no practical problem because the prevailing practice in most cases is to have parties to both premarital and postmarital agreements separately represented.

SECOND, each spouse must, at the time of execution, own property with a total net value exceeding $1.2 million. This effectively prevents all but the wealthiest couples in Minnesota from using these agreements. Even for the wealthy few who can meet the financial threshold, the statutory words, "at the time of execution" may create problems. Did the Legislature mean

"the lawyer representing a party to [a premarital] agreement is well-advised to insist that the other party be separately represented."

the moment before execution only? Did it mean before and during execution? Or is the true meaning before, during, and after execution?

Suppose, to meet the $1.2 million threshold for both spouses, one spouse transfers assets to the other, the agreement is executed, and the transferee spouse transfers the assets back. Is the agreement thus rendered invalid? Of course, the most conservative interpretation would be that the statute requires the threshold to be met before, during, and after execution. Statutory interpretation aside, there is no justification for allowing only the richest Minnesota married couples to contract with each other.

This legislation poses a new problem for married couples who are separating. If a couple does not have the required $1.2 million each, Minnesota law now declares their agreement to be invalid.

Under section 71(b)(2)(B) and section 215 of the Internal Revenue Code, payments by one spouse to the other pursuant to a written separation agreement are deductible from the payor's income and included in the payee's income. Such agreements need not be incorporated into a temporary order or a decree of divorce; the payments will be deductible or included, respectively, even if a divorce action is not pending if the parties are, in fact, separated and file separate returns. Such agreements are often used by couples for tax purposes while they negotiate an amicable divorce or legal separation.

The Tax Court has indicated that payments pursuant to an agreement executed as a result of fraud, duress, or mistake will not have the tax effect provided for by the Code.[14] An agreement executed in defiance of state law might get the same treatment from the IRS. Using such agreements probably isn't worth the risk, when parties can be certain of accomplishing the desired tax effect by commencing an action for dissolution or legal separation and stipulating to the entry of a court order requiring the payments to be made.[15]

The upshot is that Minnesotans not having $1.2 million each are now virtually required to use this more formal route. They are thus deprived of the option of using the simpler, less expensive, and private written separation agreement.

THIRD, neither party may commence an action for separation or dissolution within two years of execution of a postmarital agreement without invalidating it. The Legislature may have been trying to prevent overreaching by a spouse secretly planning divorce at the time of execution. Under existing law, a spouse who had been so deceived to his or her disadvantage would have remedies by which to invalidate such a contract or a court decree which incorporated it.[16] This requirement is therefore unnecessary. What is more, it has a distinct, perhaps unanticipated, bad feature.

A spouse who has a change of heart about a postmarital agreement may avoid it by merely commencing a separation or dissolution action within two years of execution. Commencing the action would appear to invalidate the agreement even if the action is withdrawn the next day. Thus, postmarital agreements are unstable for two years after they are made.

FOURTH, parties to postmarital agreements are forbidden to use them to determine child support, custody, or visitation. Under existing law, as all lawyers know, courts will not be bound by any agreement (premarital or postmarital) which adversely affects the rights or welfare of children. The Legislature, however, bans all postmarital agreements on these subjects whether they are bad or good for the children. For example, shouldn't a spouse be allowed, by a valid postmarital agreement, to assume responsibility for a child's college expenses or a minor stepchild's support?

FIFTH, the legislation provides that amendments to, or revocations of premarital and postmarital agreements must comply with its terms. Thus people who cannot meet the $1.2 million financial threshold under the new law are effectively precluded from revoking or amending preexisting premarital or postmarital deals.

PERHAPS the Minnesota Legislature will reflect, relent, and repeal or revise this

bad legislation. The ideal state of law would be for the well-understood requirements for premarital agreements to apply to postmarital agreements as well, perhaps with the clarification that the parties for both types of agreement must be represented by separate counsel,[17] and the explicit statutory statement that such agreements may affect children favorably, but not adversely. □

NOTES

1. E.g., *The Colorado Marital Agreement Act, Colo. Rev. Stat. §14-2-301-310 (1987).*
2. *W. Holdsworth,* A History of English Law, Vol. 5, 310-12 *(3d. ed. 1945).*
3. Id.
4. *L.M. Friedman,* A History of American Law 208 *(2d ed. 1985).*
5. Id. *at 209-10 (United States); Married Women's Property Act, 1882, 45 & 46* Vic., *ch. 75 (England).*
6. *Minn. Stat. Ann. §519.11 (1990);* McKee-Johnson v. Johnson, *444 N.W.2d 259 (Minn. 1989).*
7. Id.
8. McKee-Johnson v. Johnson, supra, *at 267.*
9. Id. *at 266.*
10. E.g., id.
11. *It provides, as well, that contracts dealing with real estate have to comply with Minn. Stat. Ann. §500.19(4) and (5)(1994) which deal with joint tenancies and tenancies in common of realty. Minn. Stat. Ann. §524.2-204 (1994) specifically authorizes postmarital agreements by which a spouse waives the right of election, rights to homestead, exempt property, and/or family allowances.*
12. *1991 WL 132760 (Minn. App.)(unpublished). The opinion does not mention Minn. Stat. Ann. §519.06.*
13. *Not explicitly. The amendment does not mention the* Lerner *case. It says that "Nothing in [M.S.A.] sections 519.01 to 519.101 shall be construed to affect antenuptial or postnuptial contracts or settlements." It specifically exempts agreements made under Minn. Stat. §524.2-204 and conveyances made under Minn. Stat. §500.19 from its requirements.* See *note 11,* supra.
14. *S. Heath, 4OTCM889, EC. 37, 139(m), TC Memo. 1980-301.*
15. *IRC §71(b)(2)(A),(C).*
16. *On the ground of fraud or mistake.* See e.g., Miranda v. Miranda, *449 N.W.2d 158 (Minn. 1989).*
17. *The authors disagree on requiring separate representation but both agree that there is no legitimate reason for distinguishing, as Minnesota law now does, between the two types of agreement.*

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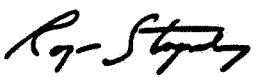

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