

[DATE]

John Smith, Esq.
123 California Street
Any Town, California 92262

RE: IRMO Jones - Notice of Fiduciary Duties
Case No.: IND-123456

Dear Mr. Smith:

I enclose herewith a Notice of Fiduciary Duties setting forth all of the statutes governing your client's fiduciary obligations to my client, which impose duties on her both during marriage and since separation, and continuing through the resolution of all property, support and attorney fee issues and the final distribution of assets. My office takes these statutes very seriously and vigorously enforces them on behalf of our clients. I send this notice so there is no issue of whether or not I have put your client on notice of our intention to require her to comply with all of them.

Fiduciary Duty Imposed by Family Code §§ 721 and 1100: Family Code §§ 721 and 1100 impose on spouses an obligation to act in the **highest good faith** and to never take **any unfair advantage** of the other when they are doing things that involve the other. This fiduciary duty includes, but is not limited to, the duty to disclose "**all material facts and information regarding the existence, characterization and valuation of all assets in which the community has or may have an interest and debts for which the community is or may be liable,**" as well as all material facts and information relating to the income and expenses of each party. Moreover, each spouse must "provide equal access to all information, records, and books that pertain to the value and character of those assets and debts, upon request."

Your client is under an obligation to disclose all material facts and information regarding the existence, characterization and valuation of assets and debts, and about her income and expenses, **without request.**

Fiduciary Duty Imposed by Family Code § 2102: Family Code § 2102 imposes the fiduciary duty described in Family Code § 721 upon both spouses as to all assets and liabilities **from the date of separation until the date the asset or liability in question is actually distributed and, as to support and professional fees, until a binding resolution is reached on these issues.** Several related issues bear emphasizing.

1. **Commencement of the Duty:** The duty commences **at the date of separation, not** the date an attorney is hired or the date a petition for dissolution is filed. Thus, your client has been under this duty for some time.
2. **Cessation of the Duty:** The duty continues “until the asset or liability has actually been distributed.” **This duty continues even after the parties have signed a settlement agreement as it relates to assets and liabilities under their respective control.**

As to child and spousal support and professional fees, this duty continues “to the date of a valid, enforceable and binding resolution of all issues relating to child or spousal support and professional fees.” This normally occurs when the case is settled. However, with regard to child and spousal support, and additional attorney fee issues, the court may continue to make orders for years after judgment. There is no case law on whether the duty continues through that period, but I assume that it does as to matters relative to support issues over which the court continues to have the ability to make orders.

3. **Requirements of the Duty:** Both parties are obligated to act in the **highest good faith** and may never take **any unfair advantage** of the other as it relates to “**all activities that affect the assets and liabilities of the other party**” and “**as to all issues relating to support and fees.**” The duty includes, but is not limited to, the full, timely, accurate and complete disclosure of:
 - a) “all assets and liabilities in which the party has **or may have** an interest or obligation,” regardless of which party owns the asset or owes the liability and **regardless of whether the asset is community or separate property;**
 - b) all current earnings, accumulations, and expenses **and “all material facts and information regarding income or expenses of the party;”**
 - c) the written disclosure of investment/business/income-producing opportunities “**in sufficient time for the other spouse to make an informed decision as to whether he or she desires to participate in the ... opportunity, and for the court to resolve any dispute regarding the right of the other spouse to participate in the opportunity;**”
 - d) the operation or management of a business, regardless of whether it is

community or separate property; and

- e) **the “immediate, full and accurate update or augmentation [of the previously disclosed information] to the extent there have been any material changes.”**

4. **Voluntary Nature of Duty:** The duty set forth in Family Code § 2102 is voluntary. **This means that your client is obligated to provide the information specified in Family Code § 2012 even though we have not asked for it.** Other duties, such as some found in Corporation Code §§ 16403 ©)(1) (which is attached hereto), are only “upon request.”

Sanctions for Violation of Family Code § 2102: Your client’s violation of any provision Family Code § 2102, **intentional or unintentional, will result in mandatory sanctions,** including those provided in Family Code § 2107©), which provides that

“(i)f a party fails to comply with any provision of this chapter, **the court shall,** in addition to any other remedy provided by law, **impose money sanctions** against the noncomplying party. **Sanctions shall be in an amount sufficient to deter repetition of the conduct or comparable conduct, and shall include reasonable attorney’s fees, costs incurred, or both,** unless the court finds that the noncomplying party acted with substantial justification or that other circumstances make the imposition of the sanction unjust.” (Emphasis added).

In essence, the court is required to order the party violating § 2102 to pay the reasonable attorney and expert fees incurred by the other party as a result of the violation, **and** to impose a form of punitive damages in the nature of “money sanction” unless there was “substantial justification” or “other circumstances” which makes the sanction unjust.

Requirements of the Corporation Code: Three sections of the Corporations Code, which are portions of the Uniform Partnership Act, are incorporated by reference into Family Code § 721 and therefore are applicable to your client. While numerous obligations are addressed in these code sections, I want to stress to you the importance of the following:

1. **The “Duty of Loyalty:”** Corporations Code § 16404(b) creates a duty of loyalty” between “partners,” which in a family law context means between spouses. The duty of loyalty requires the spouse to “account” to the other spouse and “hold as a trustee” for profits made during the marriage and the “winding up” (dissolution) of the marriage.

Although this section has not been interpreted in a family law context, in a partnership context, **this section also prohibits spouses, prior to separation, from competing with the community in investment opportunities** (often referred to as “usurping a community opportunity”). Family Code § 2102, discussed above, applies to investment-type opportunities after separation. Under either section, the violation of the prohibitions results in the investment being deemed community property under most circumstances.

The concept of usurping a community opportunity usually arises when one spouse is presented with an investment or similar income-producing opportunity and takes advantage of it with separate funds rather than community funds. In most circumstances, but not all, such conduct violates the community opportunity doctrine, resulting in a breach of the fiduciary duty. **We will investigate the use of any of your client's separate property during marriage and since separation to determine whether we feel she has violated this duty.**

2. **The "Duty of Care:"** Corporations Code § 16404(c) creates a "duty of care" between partners/spouses. The duty is to refrain from engaging in "grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law." This duty of property, including making investments and operating a business. We recognize that the duty of care is governed by the "Business Judgment Rule" which provides that in the management and control of partnership activities, a partner need only satisfy a standard of care demanded of an "ordinarily prudent clarity of hindsight." It is presumed that partners abide by the Business Judgment Rule. However, where a partner has a conflict of interest, the presumption does not apply and it is the partner's duty to establish that he or she has acted in a manner consistent with the rule. By incorporating Corporations Code § 16404 into Family Code § 721(b), it appears that the Business Judgment Rule is also the guiding light for spouses in the management and control of community property.

We will be investigating your client's conduct in managing community assets to determine whether we feel she has violated this duty.

3. **The Duty of Good Faith and Fair Dealing:** Corporations Code § 16404(d) provides that the duty owed between spouses/partners is one of good faith and "fair dealing." However, this section is incorporated into Family Code § 721(b) which provides that the spouses owe "a duty of **the highest good faith and fair dealing**" and that "**neither spouse shall take any unfair advantage of the other.**" The duty in Family Code § 721(b) appears to be a higher standard than the one in Corporations Code § 16404(c), but no case has addressed this issue. The duties certainly mean, however, that all actions taken with respect to the dissolution action and the community estate must be done fairly and with the other party's rights and interests in mind. **We will vigorously enforce your client's obligation in this respect both during marriage and since separation.**
4. **The Duty to Provide Information:** Corporations Code § 16403(c) requires a spouse/partner to provide **without demand** "any information" concerning the partnership/community business and affairs "**reasonably required for the proper exercise of the partner's [spouses] rights and duties under the partnership agreement [Family Code].**" Pursuant to Family Code § 1100, either spouse has the management and control of the community property and must exercise that management and control consistent with the fiduciary duties described in this letter.

While no case has addressed this issue in a family law context, when this mandate is combined with the provisions of Family Code § 2102, it is likely that “any information” required for the proper management and control by of community property by either spouse **must be provided voluntarily**.

In addition, **on demand**, “**any other information concerning the partnership business and affairs**” must be provided unless otherwise improper or unreasonable. This mandate is consistent with the requirements of Family Code §§ 721, 1100(e) and 2102. **By separate letter, we will demand that your client fully comply with all of her voluntary disclosure obligations and also that she fully disclose all information which she is obligated to do upon request.**

Setting-Aside Settlement Agreement for Breach of Duty: In addition to the sanctions discussed above, Family Code § 2122(f) provides that any settlement agreement which we enter into may be set aside as a result of the failure to comply with **all disclosure requirements**, including those discussed in this letter. Family Code § 2122(f) provides a settlement agreement may be set aside for:

“(f)ailure to comply with the disclosure requirements of Chapter 9 (commencing with Section 2100). [This includes the provisions of Family Code § 2102.] An action or motion based on failure to comply with the disclosure requirements shall be brought within one year after the date on which the complaining party either discovered, or should have discovered, the failure to comply.”

It would be unwise to enter into a settlement agreement only to have it set aside because of your client’s failure to honor her fiduciary duty. Our goal, therefore, is to provide and exchange information early in the process in order to facilitate settlement to the extent possible.

Declaration of Disclosure Requirements: Family Code §§ 2104 and 2105 set forth the requirements to provide a Preliminary Declaration of Disclosure (“PDD”) and Final Declaration of Disclosure (“FDD”). We have already complied with all of those requirements and will enforce your client’s obligation to do the same.

The above statutes impose upon your client the duty of “**immediate, full and accurate update or augmentation** [of the previously disclosed information] **to the extent there have been any material changes.**” It is vital that she understand this obligation so that any changes in her financial situation are disclosed immediately.

Perjury and Subornation of Perjury: Finally, it is important to understand the definition of perjury includes not only a declaration which “**states as true any material matter which he or she knows to be false**” (Penal Code § 118) but also “**(a)n unqualified statement of that which one does not know to be true is equivalent to a statement of that which one knows to be false.**” (Penal Code § 125).

Thus, if your client states in the FDD or the waiver thereof that “**all** material facts and

information” are or have been disclosed and she knows that “**all**” material facts have not been disclosed or is not sure that “**all**” material facts have not been disclosed, she may be committing perjury. Perjury is grounds for setting aside the judgment settling the case. In this context, please review Penal Code § 127 as it relates to subordination of perjury.

I have enclosed a copy of the Notice of Fiduciary Duty which will be filed with the Court. I ask that you provide your client’s preliminary declaration of disclosure and file the Declaration Regarding Service of Declaration of Disclosure within 20 days. If you fail to do so, we will pursue all legal remedies to bring this case to its conclusion.

Very truly yours,

THURMAN W. ARNOLD, III

TWA:dd
Enclosure
cc:Client