No. 17–521

In the Supreme Court of the United States

CAROLYN LAZAR,
Petitioner,
v.
MARK G. KRONCKE, IN HIS CAPACITY AS ADMINISTRATOR OF THE ESTATE OF GEORGE THOMAS KRONCKE,
Respondent

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITIONER'S REPLY BRIEF

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INTRODUCTION

Respondent cannot obscure the need for this Court's review. Neither respondent nor Arizona disputes that there is a mature, acknowledged split over whether the Contracts Clause bars applying revocation-on-divorce statutes retroactively. Nor do they dispute that the lack of clarity caused by the split is important, clouding title to non-probate assets held by millions of Americans and worth trillions of dollars. As amici women's groups explain, the issue threatens women's retirement security, exacerbating their financial vulnerability. And Arizona itself is now before the Court to defend its statute, making this case an even better vehicle.

Instead, respondent and Arizona improperly ask the Court to deny review based on arguments never made before, relying on contested allegations outside the pleadings and not considered by the courts below. Indeed, these new arguments are the *sole* basis for Arizona's opposition to certiorari. The pure legal issue here was argued and decided on motions to dismiss, based strictly on the allegations of the First Amended Complaint and Second Amended Answer and Cross-Claim. The case was decided on the pure question of law that was pressed and passed upon below and is squarely presented here.

Respondent's new contention that the Contracts Clause does not protect trusts is erroneous under this Court's precedent. Thus, it does not distinguish this case from the others in the 4–2 split. And respondent's remaining contention—that the account holder's right to designate a beneficiary is not an element of the contract—is part of the question presented that only this Court can resolve. Further review is warranted.

ARGUMENT

I. THE POSTURE OF THIS CASE, DECIDED ON A MOTION TO DISMISS AS A PURE QUESTION OF LAW, MAKES IT A CLEAN VEHICLE

1. This case remains a clean vehicle, now made even more suitable by Arizona's intervention to defend its statute. The parties and courts below resolved the question presented as a pure question of law on motions to dismiss, based on five facts alleged in the First Amended Complaint and Second Amended Answer:

(1) In 1992, Tom Kroncke opened an individual retirement account (IRA) and designated Carolyn Lazar as his beneficiary;

(2) In 1995, Arizona passed its revocation-on-divorce statute;

(3) In 2008, Carolyn and Tom divorced;

(4) In 2012, Tom died; and

(5) From 1992 until Tom's death in 2012, Carolyn remained the primary beneficiary of that account.

Pet. App. 2a, 28a; CA9 E.R. 428–29, 780.

That is all that was properly before the courts below, and now this Court, on a motion to dismiss. In that posture, a court may not rely on "matters outside the pleadings" without first giving the parties notice and converting it to a motion for summary judgment. Fed. R. Civ. P. 12(d).

Respondent and Arizona have never contested these five facts, but seek to inject additional allegations that they claim undermine petitioner's rights: a

2001 unauthenticated document that named a different contingent beneficiary but kept petitioner as the primary beneficiary, and a 2008 Property Settlement Agreement. Neither is relevant to the decision below: as respondent concedes, the court below "was not asked to decide that . . . Arizona's 1995 ROD statute does not impair the subsequent 2001 beneficiary designation or 2008 Property Settlement Agreement." Opp. 13. Rather, it focused exclusively (and appropriately) on the 1992 contract. If either of the two later documents would have supported a decision in respondent's favor, surely respondent would have brought them front and center. He would not have argued against producing them and spent four years litigating the constitutionality of applying the revocation-on-divorce statute to the 1992 contract, with no mention of these later documents.

Given that "[t]he instant case was considered below on a motion to dismiss," any "conflicting assertions on this matter are not before" this Court. *Cutter* v. *Wilkinson*, 544 U.S. 709, 725 n.13 (2005). "Because these defensive pleas were not addressed by the Court of Appeals, and mindful that [the Supreme Court is] a court of review, not of first view," this Court "do[es] not consider [such defensive pleas] here." *Id.* at 718 n.7.

2. Moreover, the district court "granted the Estate's motion to stay discovery after concluding that the motion to dismiss raises only legal issues, is potentially dispositive of the entire case, and is not dependent on additional fact discovery." Pet. App. 30a. Having opposed full investigation of matters beyond the pleadings, respondent cannot do an about-face and not only raise but rely on them here. Schwab's

counterclaim referenced and attached only the 1992 beneficiary designation of Lazar, not the 2001 document, and respondent's answer never raised it either. CA9 E.R. 793, 798–99. Even if this argument were not waived, neither the validity of these extra-record documents nor their correct interpretation has ever been addressed.

3. As to the 2008 Property Settlement Agreement cited by respondent, it never mentions Tom's designation of Carolyn as primary beneficiary of the IRA, let alone purports to waive it. It simply divided current assets, giving Carolyn a fraction of the IRA immediately but leaving her as primary beneficiary. Neither respondent nor the lower courts argued or addressed the 2008 agreement before now, and it has no bearing here.

This Court should decide the important legal question presented on the pleadings, as the courts below did. It should reject respondent's (and Arizona's) attempt to invent a vehicle problem based on extraneous factual allegations and legal theories that have not been adjudicated and are irrelevant to the purely legal question presented.

II. LIKE OTHER NON-PROBATE ASSETS, IRA AGREEMENTS ARE CONTRACTS, AS RESPONDENT ARGUED BELOW

Respondent asserts that an IRA, as a type of trust, "is not a contract within the meaning of the Contracts Clause." Opp. 9. For that reason, he (but not Arizona) argues (at Opp. 6) that this case differs from all the other cases cited in the petition that have addressed revocation-on-divorce statutes, *see* Pet. 9–13, and that the court of appeals was correct in finding no Contracts Clause violation (Opp. 12).

Respondent never advanced this argument in any court below. This Court itself has rejected respondent's premise, as have other cases and authorities. It is contrary to the holding of the court of appeals and has never been adopted by any other court in this context. Respondent's new "no-contract" argument provides no basis to deny review.

1. Respondent concedes that he has never before advanced his current argument that the IRA agreement is not a "contract for purposes of the Contracts Clause." Opp. 9, 13. He acknowledges that the Ninth Circuit "was not asked to decide that an IRA is a trust rather than a contract." *Id.* at 13. That alone should foreclose consideration of this argument.

2. In any event, this Court has squarely rejected respondent's new position. In *Coolidge* v. *Long*, the Court held that "trust deeds are contracts within the meaning of the contract clause of the Federal Constitution." 282 U.S. 582, 595 (1931). The Court explained that, under the Contracts Clause, a State is "without authority by subsequent legislation, whether enacted under the guise of its power to tax or otherwise, *to alter their effect* or to impair or destroy rights which had vested under them." *Id.* (emphasis added).

Lower federal courts have also acknowledged that "IRAs and insurance policies are contracts between the owner and the company issuing the account or policy." *Maccabees Mut. Life Ins. Co.* v. *Morton*, 941 F.2d 1181, 1185 (11th Cir. 1991); *see also Williams* v. *Interpublic Severance Pay Plan*, 523 F.3d 819, 821 (7th Cir. 2008) ("Trust law honors rather than over-

rides express contractual language specifying a trustee's powers vis-à-vis a beneficiary.").

State supreme courts agree. *See*, *e.g.*, *Crawford* v. *Barker*, 64 So. 3d 1246, 1253 (Fla. 2011) ("An IRA is a contract with an institution that involves a third-party beneficiary designation.") (quoting *Luszcz* v. *Lavoie*, 787 So. 2d 245, 248 (Fla. Dist. Ct. App. 2001)); *Alexander* v. *McEwen*, 239 S.W.3d 519, 522 (Ark. 2006) ("An IRA constitutes a contract between the person who establishes the IRA for his or her retirement and the financial institution that acts as the custodian for the IRA.") (citing *Smith* v. *Smith*, 919 So. 2d 525 (Fla. Dist. Ct. App. 2006)). A leading authority on the law of trusts also agrees that "the deal between settlor and trustee is functionally indistinguishable from the modern third-party-beneficiary contract. *Trusts are contracts*." John H. Langbein, *The Contractarian Basis of the Law of Trusts*, 105 Yale L.J. 625, 627 (1995) (emphasis added). And a trust's status as a contract is not a matter of Arizona law, but rather "a federal question for purposes of Contracts Clause analysis." *General Motors Corp.* v. *Romein*, 503 U.S. 181, 187 (1992) (citing *Irving Tr. Co.* v. *Day*, 314 U.S. 556, 561 (1942)). *Contra* Opp. 8.

Respondent's new-found argument, therefore, has no merit. Tom's contract with Schwab is a contract that created rights protected by the Contracts Clause. Because the courts are divided on whether those rights were violated, further review is warranted.

3. Respondent's new argument also contradicts his arguments in the courts below and the court of appeals' holding.

a. In the Ninth Circuit, respondent argued that IRAs contain a mix of contractual and "donative elements," and that the beneficiary designation is a "donative element" not protected by the Contracts Clause. *See* Appellee's CA9 Answering Br. 45, 47 ("[R]evocation-on-divorce statutes do not impair any contractual rights because they address only the 'donative transfer' elements of such agreements."); Opp. 13–17. That position was premised on the understanding that the IRA agreement *was* a contract, within which the beneficiary designation was a "donative element."

b. Respondent's new argument also contradicts the court of appeals' holding. Agreeing with respondent's argument at that time, the court of appeals explained that "[t]he Decedent's *contract* with Schwab specified that Schwab would pay his chosen beneficiary in the event of his death," but that—in its view—the "beneficiary designation itself was not a contractual term." Pet. App. 18a–19a (emphasis added). Each of the other revocation-on-divorce decisions accepts that a contract is involved. In agreeing with respondent, the court of appeals recognized that it was taking a firm position on an issue that had already divided the courts of appeals and state supreme courts. *Id.* at 17a–18a. Only this Court can resolve the conflict. *See* Pet. 14.

4. Because trust agreements are contracts protected by the Contracts Clause, respondent's attempt to distinguish cases in the circuit split involving other types of contracts is misguided. First, respondent's stated premise—that "all . . . involved insurance policies," Opp. 6 (citing Pet. 9–11), is wrong. Several cases in the conflict dealt with retirement

vehicles similar to IRAs, including *Stillman*, which involved annuities, and *Storsve*, which involved state retirement accounts. *See Stillman* v. *Teachers Ins. & Annuity Ass'n Coll. Ret. Equities Fund*, 343 F.3d 1311, 1312 (10th Cir. 2003); *Buchholz* v. *Storsve*, 740 N.W.2d 107, 109 (S.D. 2007). While neither found a Contracts Clause violation, *Stillman* and *Storsve* agreed that those types of non-probate assets involved contracts within the meaning of the Contracts Clause. *See*, *e.g.*, *Stillman*, 343 F.3d at 1313 (describing "the annuity *contracts*" at issue) (emphasis added).

Moreover, the authority respondent himself cites confirms that IRAs are no different from insurance policies, retirement accounts, or other non-probate assets with beneficiary designations. Respondent argues that non-probate assets (which he relabels "will substitutes") are categorically not "contractual arrangements" subject to the Contracts Clause. Opp. 10 (quoting Restatement (Third) of Prop.: Wills and Donative Transfers § 7.1(a) cmt. a (Am. Law Inst. 1999)). These non-probate assets include "life insurance, *pension and employee-benefit accounts*, . . . and annuities with death benefits." *Id.* (omission in original) (emphasis added). He adds: "The category of pension and employee-benefit accounts *includes* IRAs." *Id.* (quoting § 7.1 cmt. d. (emphasis added)). Q.E.D.

Accordingly, whatever argument respondent is now making would apply equally to all of the non-probate assets at issue. Each of the courts has recognized that the non-probate assets at issue involve a contracting party, a financial firm, and a beneficiary. Each of the decisions on both sides of the con-

flict (including the Ninth Circuit's decision here) would apply to all of the non-probate assets that respondent lists. No court has suggested any distinction among them that would affect the Contracts Clause analysis.

III. THE CONTRACTS CLAUSE BARS NULLIFYING BENEFICIARY DESIGNATIONS RETROACTIVELY

1.a. Non-probate assets are created by contracts between account holders and financial institutions, as respondent and the Ninth Circuit acknowledged below. Pet. App. 18a; Appellee's CA9 Answering Br. 47. It is irrelevant whether Carolyn's rights were "vested." Opp. 16–17; Pet. App. 18a. Tom had a contract with Schwab, and Carolyn has third-party standing to enforce Tom's contract. Pet. App. 15a–16a; Restatement (Second) of Contracts §§ 302(1) & illus. 4 (Am. Law Inst. 1981). "What matters are the policyholder's rights and expectations, not any interest of the beneficiary." *Metro. Life Ins. Co.* v. *Melin*, 853 F.3d 410, 413 (8th Cir. 2017), *petition for cert. filed sub nom. Sveen* v. *Melin*, No. 16–1432 (June 1, 2017).

b. Revocation-on-divorce statutes abrogate contractual rights and obligations. *Contra* Pet. App. 18a–19a; Opp. 14–16. Tom designated Carolyn as primary beneficiary to ensure that if he died, she would be taken care of financially. Agreements governing the disposition of non-probate assets are not merely donative, but contractual; those aspects are not severable. Account holders are entitled to rely on financial institutions to carry out their written instructions. If financial institutions disregard those instructions and disburse money to the wrong per-

son, they can be sued for breach of contract. Pet. 16–17.

c. Revocation-on-divorce statutes "go[] too far" by "disrupt[ing] settled and completed financial arrangements made in reliance on existing law." *Whirlpool Corp.* v. *Ritter*, 929 F.2d 1318, 1323 (8th Cir. 1991) (quoting *Minn. Ass'n of Health Care Facilities, Inc.* v. *Minn. Dep't of Pub. Welfare*, 742 F.2d 442, 451 (8th Cir. 1984)). An account holder is entitled to "rely on the pre-existing law and neither know nor expect that the rules governing his [account] have changed." *Id.*

2. It does not save these statutes to claim that they merely provide an "intent-serving default rule." Opp. 20 (quoting Opp. App. 3). Account holders usually will not learn that legislatures have passed such statutes and so will not know they must redesignate their beneficiaries. Thus, these "statute[s] [are] just as likely to 'either effectuate or frustrate [the decedent's] intent.'" *Melin*, 853 F.3d at 413 (quoting *Whirlpool*, 929 F.2d at 1323). "As in contract law generally, the best evidence of the parties' intent is found in the written documents that they executed." Amici Br. 13. Even if some account holders might not mind the change, that cannot justify nullifying the written beneficiary designations relied on by others.

Respondent argues that "[t]here is no U.S. Supreme Court authority for the . . . extension of Contracts Clause regulation to legislative default rules." Opp. 21 (quoting Opp. App. 5). But neither is there any rationale for treating "legislative default rules" differently from any other legislation for Contracts Clause purposes, and respondent has offered no authority to the contrary. Respondent's argument ac-

tually reinforces the need for guidance from this Court to end the confusion in the lower courts on the question presented, especially considering its practical impact on trillions of dollars in non-probate assets.

3. Finally, even if Arizona could meet its burden of proving that its revocation-on-divorce statute had a "significant and legitimate public purpose," it cannot show that it is based on "'reasonable conditions'" and is "'appropriate'" to serve that purpose. *Energy Reserves Grp.* v. *Kan. Power & Light Co.*, 459 U.S. 400, 411–12 (1983) (quoting *U.S. Tr. Co.* v. *New Jersey*, 431 U.S. 1, 22 (1977)). There are alternative solutions that would be less destructive of contract rights than nullifying beneficiary designations automatically, retroactively, and without warning. For instance, the Pension Rights Center and National Women's Law Center have suggested automatically sending a new beneficiary designation form to account holders upon notice of divorce. Pension Rights Ctr. & Nat'l Women's Law Ctr., Comments to ERISA Advisory Council 5 (2012), https://perma.cc/S8D7-CBJT. Additionally, financial institutions could send beneficiary designation forms to account holders each year, prompting them to consider how divorce and other family changes might influence their estate planning. States could require investment firms (or divorce courts) to notify parties to a divorce that they may wish to reconsider beneficiary designations. Legal ethics rules could require attorneys to make the same notifications to their clients. Finally, States could draft these laws to apply only prospectively, as Oklahoma has done. Pet. 21 n.3. There is no significant or legitimate need to nullify

written beneficiary designations, which are the best indication of account holders' intent.

* * * * *

This is the ideal vehicle for resolving the circuit split on this important, recurring issue. Arizona's Solicitor General has intervened to defend the State's interest, and seven major national and state organizations have explained the importance of protecting women's financial security in retirement. Retirement accounts in particular often represent both spouses' contributions to earning and saving together over the course of a marriage, even if it ends in divorce. Millions of Americans rely on such accounts, which contain trillions of dollars, for retirement security. While this issue remains unresolved, protracted litigation drains accounts, freezes trading in account assets, and wreaks havoc with ex-spouses' retirement planning. The time is ripe to bring much-needed clarity to this important area of the law.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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November 16, 2017