Estate Planning
For
Community Property

Bar Association of San Francisco

May 11, 2017

Presented by:
Harry B. Maring
Attorney at Law
456 Montgomery Street, Suite 1300
San Francisco, CA 94104
(415) 989-8406
hmaring@maringlawfirm.com
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Family Facts

HARVEY - 65  

WYNONA - 45  

Joint Children  
Sean - 5  
Sally - 2  

Children From Prior Relationships  
Charles - 45  
Charlotte - 42  
Chris - 40  
Fannie - 15  

General Fact Pattern

When HARVEY and WYNONA got married, HARVEY’s property was valued at $7 million:

House then worth $2 million with a $1 million mortgage ........................................ $1.0M  
Cash and liquid investments ................................................................. $2.0M  
Company 401(k) ................................................................................. $2.0M  
Concert promotion business .................................................................. $1.0M  
Real estate $1 million ........................................................................... $1.0M  
Total Value ......................................................................................... $7.0M  

Today, the values are:

House worth $3 million with a $.5 million mortgage ........................................... $2.5M  
Cash and liquid investments ......................................................................... $3.0M  

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WYNONA had a checking account with a few hundred dollars in it when they got married.

HARVEY and WYNONA have walked into your office for an estate planning consultation.

All parties have been California residents for their entire lives.

**Community Property Issues**

The goal of this presentation is to alert the planner to the problems of characterizing separate property and community property in order to determine which spouse has control over which assets or the amount of assets they have control over.

Try to decide what is community property and what is separate property in each of the following situations:

**Fact pattern 1**
Wife has $1.5M she inherited and keeps in an account in her own name. She deposits her earnings into this account. H&W buy a house in joint names and use part of this money as a down payment. H&W earnings go to pay the mortgage.

**Fact pattern 2**
Wife owned the condo before marriage. Wife is now married. H&W use joint earnings to pay on mortgage. Wife sells condo and reinvests proceeds in a new house which is in both names and both are on the mortgage.

**Fact pattern 3**
H owned house before marriage. There is no debt on the house. H is going to put the house into joint names with wife.

**Community Property Issues with Real Estate**

House brought into marriage - no debt
House brought into marriage - with debt
House brought into marriage and converted to joint names
House bought during marriage in one person's sole name using their separate property - no debt
House bought during marriage in one person's sole name using their separate property - with debt
House bought during marriage in joint names using one person's separate property - no debt
House bought during marriage in joint names using one person's separate property - with debt

Brief History of California Community Property

California became the 31st state of the United States when President Millard Fillmore signed the bill for admission on September 9, 1850.

California's marital property law is based upon the community property system, dating back to the adoption of the state's first Constitution in 1849, when the constitutional convention opted to perpetuate the community property system of the Civil Law of Spain and Mexico in the legal system of California.

The 1849 California Constitution, Article XI, Section 14 provides:

All property, both real and personal, of the wife, owned or claimed by her before marriage, and that acquired afterwards by gift, devise or descent, shall be her separate property; and laws shall be passed more clearly defining the rights of the wife, in relation as well to her separate property, as to that held in common with her husband. Laws shall also be passed providing for the registration of the wife's separate property.

Thus, from the very beginning, it can be seen that a process of classifying or characterizing property as separate or as common was necessary.

Characterization

Characterization of property, for the purpose of community property law, refers to the process of classifying property as separate, community, or quasi-community. Characterization must take place in order to determine the rights and liabilities of the parties with respect to a particular asset or obligation and is an integral part of the division of property on marital dissolution. Generally, factors determinative of whether property is separate or community are the time of the property's acquisition; operation of various presumptions, particularly those concerning the form of title; and whether the spouses have transmuted or converted the property from separate to community or vice versa. Perhaps the most basic characterization factor is the time when property is acquired in relation to the parties' marital status. In re Marriage of Haines, 33 Cal.App.4th 277, 39 Cal.Rptr.2d 673 (1995) at page 291.

Thus, we need to be aware of when the property was acquired, what presumptions apply, what was the form of the title in which the property was acquired and were there any agreements that changed the character of the property.
Tracing

The concept of tracing is very important to the community property system. Tracing is the concept whereby if you can identify the source of the funds used in the transaction, that may have an important impact on the person trying to establish whether the property is separate or community. George v. Ransom, 156 Cal. 322 (1860).

Community Property Definitions

Family Code Section 760 gives us the starting point for the current discussion of Community Property:

Except as otherwise provided by statute, all property, real or personal, wherever situated, acquired by a married person during the marriage while domiciled in this state is community property.

This definition treats the spouses equally, regardless of whose labor generated the means to acquire the property and regardless of the contribution of either party to the cost of acquisition.

On the other hand, separate property is defined under Family Code Section 770 as:

(a) Separate property of a married person includes all of the following:

(1) All property owned by the person before marriage.

(2) All property acquired by the person after marriage by gift, bequest, devise, or descent.

(3) The rents, issues, and profits of the property described in this section.

(b) A married person may, without the consent of the person's spouse, convey the person's separate property.

Thus, property meeting the definition of separate property is an exception to the general rule of Family Code Section 760 where an acquisition during marriage is community property.

Family Code Section 760 characterizes any property acquired during marriage as community property. However, the case of Estate of Clark, 94 Cal. App. 453, 271 P. 542 (1928) reiterates the holding in George V. Ransom above, and states that the separate property proponent can trace the funds used to make the acquisition to his or her separate property to show that the asset in question, is his or her separate property because it fits into one of the three categories of Family Code Section 770.
Presumptions

The law has established certain presumptions that help to guide us in the characterization process. Certain presumptions are either conclusive and not rebuttable by additional facts while others are rebuttable if the proper facts are presented.

However, an important NOTE: The General Community Property Presumption under Family Code Section 760 about acquisition will apply only when the property is NOT TITLED in either spouse's name such as a ring or expensive rug or when the property is acquired during marriage and is TITLED ONLY IN ONE OF THE SPOUSES'S NAME.

If the property is titled in both names as joint tenants (with rights of survivorship), tenants in common, as husband and wife, or as community property, then the General Community Property Presumption DOES NOT APPLY - there are other presumptions that apply which have different rules and results and will be discussed below.

The General Community Property Presumption of Family Code Section 760 reflects that property acquired during marriage will, at first, be presumed to be community property, subject to an evidentiary rebuttal that it comes within a certain exception - the major exceptions to the basic community property rule are those relating to separate property and title. If evidence is presented that shows that the property is not community property, then the general presumption is rebutted.

The person trying to rebut the presumption that the property is community property is called the "separate property proponent". The separate property proponent has the burden of showing that it is separate property. If the separate property proponent cannot show that it is separate property, then the community property presumption becomes conclusive and the property is deemed to be community property.


> The character of property as community or separate is normally determined at the time of its acquisition. This is particularly true because of the general presumption that property acquired during marriage by either husband or wife or both while domiciled in California is community property, except as otherwise provided by statute. This rule can be altered by agreement of the spouses. For example, spouses can indicate their intent with respect to the character of the property initially by specifying the form of title in which it is held, or spouses can later transmute the character of the property as between each other. Where property status cannot otherwise be proved, characterization is determined by applicable presumptions. 33 Cal.App.4th at page 291.

Here, the concept of tracing will assist in rebutting the presumption - if the General Community Property Presumption is raised because the property was acquired (or possessed) during marriage, the separate property proponent can prove by TRACING that the source of funds used in the acquisition came from separate property. If that is the case, it is sufficient to rebut the presumption.
Think about it - you go out and buy a car, and most likely, you will put title in your name alone. But you wrote the check from the joint account where you and your spouse deposit your earnings every paycheck. It would be too easy to go out, use community property to buy the car in your name, then file for dissolution and claim that the car was yours alone! You can not unilaterally appropriate community property for your own use.

**Effect of How the Property Is Titled**

One could perhaps say that the form of title creates some type of rebuttable presumption of character but it may be more accurately stated that with joint forms of title, these indicate, initially, an AGREEMENT of the parties as to the character of the property.

And, to rebut the title form of ownership, another agreement or something that looks like an agreement is necessary.

**Acquisition of Title in Joint Names**

We will now focus on the nature of the title, the reason for the nature of the title and the different way that rebuttal is required.

Husband and Wife can hold title in joint names as joint tenants, as tenants in common, as community property and as community property with rights of survivorship. Family Code Section 750.

Prior to 1970, when California had a fault divorce concept, title was very important - if taken as joint tenants or tenants in common, the court could only award the property 50-50 to the spouses because their interests were held as separate property. If title was held as community property, the court could award the innocent spouse a greater percentage of the community property.

Additionally, if the home was community property, the court could award it to the wife for the use of the children - if the property was not community property, then it was the separate property of the couple and the court could not touch it.

But, with the advent of no-fault divorce in 1969 (see Family Code Sections 2310 and 2335), the court must divide the community property on a mandated 50-50 division under Family Code Section 2550.

California case law is well established that joint tenancy and community property cannot co-exist simultaneously. In Tomaier V. Tomaier, 23 Cal. 2d 754, 758, 146 P. 2d 905 (1944) at page 758, the court stated: If the evidence establishes that the property is held as community property, however, it cannot also be held in joint tenancy, for certain incidents of the latter would be inconsistent with incidents of community property.

Make sure that you check the original deed of acquisition to determine if title was taken as joint tenants or even as tenants in common to determine if you need to do a new deed reciting that it is community property at the same time as you are funding their trust.
Before 1984, where we have some form of joint title, rebuttal by tracing is not enough; the separate property proponent must show an agreement, oral or written, that the title does not control the character of the property. (Note the discussion below regarding no oral transmutation agreements after 1984 under Family Code 852 and joint title under Family Code Section 2581).

**Lucas v. Lucas**

One of the most important cases dealing with the joint form of title and the rebuttal thereof is *In re Marriage of Lucas*, 27 Cal.3d 808, 166 Cal.Rptr. 853, 614 P.2d 285 (1980).

Lucas involved a husband and wife who purchased a SINGLE FAMILY RESIDENCE in JOINT TENANCY with the wife making the down payment with her separate funds and the community made the payments on the mortgage. Upon divorce, the court was faced with the dilemma of characterizing the separate and community property components of the transaction. The Lucas court stated at page 814:

> The presumption arising from the form of title is to be distinguished from the general presumption set forth in Civil Code section 5110 (now Family Code Section 760) that property acquired during marriage is community property. It is the affirmative act of specifying a form of ownership in the conveyance of title that removes such property from the more general presumption. It is because of this express designation of ownership that a greater showing is necessary to overcome the presumption arising therefrom than is necessary to overcome the more general presumption that property acquired during marriage is community property. In the latter situation, where there is no written indication of ownership interests as between the spouses, the general presumption of community property may be overcome simply by tracing the source of funds used to acquire the property to separate property. It is not necessary to show that the spouses understood or intended that property traceable to separate property should remain separate.

The act of taking title in a joint and equal ownership form is inconsistent with an intention to preserve a separate property interest. Accordingly, the expectations of parties who take title jointly are best protected by presuming that the specified ownership interest is intended in the absence of an agreement or understanding to the contrary. 27 Cal. 3d at page 815.

Thus, it was held that the wife had made a gift to the community because there was no agreement, oral or written, to rebut the form of title.

**Reimbursement**

Family Code Section 2640

Now the Lucas court turned to the issue of whether the wife could receive reimbursement for her separate property contribution to the acquisition of the property.
The court noted at page 812 that "Wife also testified that they had no agreement regarding the manner in which she would be disposing of the trust funds and that they did not discuss keeping the funds separate or using them to exhaust community debts. Wife also testified that it was her intention at the time of the purchase to acquire the house for herself but that she did not discuss this with her husband". At page 816. Thus, not only was the wife unable to rebut the community property presumption arising from the joint tenancy form of title, she also was not entitled to reimbursement for her separate property contribution to the acquisition of the house - there was no agreement regarding reimbursement.

The Supreme Court in Lucas had resolved a conflict among the appellate divisions - however, the family law bar saw this result as totally unfair and mobilized their forces to convince the Legislature to change this result by statute.

Legislation was introduced to address the joint title issue as well as the reimbursement issue and in 1983, Civil Code Sections 4800.1 (now Family Code Sections 2580 and 2581) and 4800.2 (now Family Code Section 2640) were enacted, effective January 1, 1984.

Newly enacted Civil Code Section 4800.1 (now Family Code Section 2581) expanded the presumption to cover ALL property (not just single family residences) acquired during marriage in JOINT TENANCY form in an effort to ensure application of the community property presumption to marital property held in joint tenancy form.

Additionally, the new Civil Code Section 4800.1 provided that in order to rebut the community property presumption regarding joint tenancy, the separate property proponent must show that there was a written agreement that the property was not to be community property or that there was a statement in the deed stating that the property was not community property.

This was a new twist because prior to 4800.1, an oral statement was sufficient to rebut the presumption that title to the property controlled.

Note that the statute did not cover property acquired as tenants in common. However, this was remedied effective January 1, 1987 when all property acquired during marriage in any JOINT FORM was deemed to be community property.

In re Marriage of Hilke 4 Cal.4th 215, 14 Cal.Rptr.2d 371 (1992) at page 222 also gives us the conclusion that the joint form of title can be applied retroactively without a deprivation of due process that takes away a vested property right.

Family Code Section 2640 (former Civil Code Section 4800.2) was enacted and indicates that, unless the right was waived, a spouse who contributed their separate property to the acquisition of community property in joint names would be entitled to a dollar for dollar reimbursement for such contribution, as long as they could trace the contribution to a separate property source. Also, Family Code Section 2640(c) was added in 2004 which allows a separate property contribution to the other spouse’s separate property to be reimbursed, dollar for dollar.
Note that the reimbursement is limited to reimbursement of separate property contributions to expenditures that go to enhance the equity of a property that is community property or for improvements (see the discussion below regarding improvements), not items that are merely expenses of maintenance and upkeep. Also note that in essence, the separate property contribution is like an interest free loan to the community - it is reimbursed dollar for dollar.

But, this section does not apply to reimbursements for contributions of community property to separate property. (See the section on Apportionment and Moore/Marsden below).

Note that when one spouse who owned property as separate property prior to marriage executes a deed after marriage putting the property into joint names with the other spouse, this is treated as an acquisition during marriage. The Family Code Section 2581 community property presumption applies and if the separate property proponent can not rebut with a writing or statement in the deed, it is community property with a Family Code Section 2640 right of reimbursement to the separate property proponent if he/she can trace to a separate property source. See In Re Marriage of Weaver, 127 Cal.App.4th 858, 26 Cal.Rptr.3d 121 (2005).

Retroactivity

As a final note, the legislature tried on numerous occasions to have 2581 and 2640 applied retroactively; however, in a long line of cases such as Buol, Fabian, Hilke and Heikes, the court came to the following conclusions:

As to the retroactive application of the joint forms presumption as community property, it was held that it could be applied retroactively since there was no impairment of a vested right - if the parties had acquired the property in joint names, then the presumption does not change ownership, it was always held 50-50.

As to the requirement of a writing under 2581 to rebut the community property presumption, it was held that it could not be applied retroactively because it would impair oral agreements for reimbursement that had been made prior to January 1, 1984. If this were allowed, the wife in Lucas would have received nothing if she had an oral agreement for reimbursement.

As to the retroactive application of the right of reimbursement under 2640, it was held that this was an impairment of a vested property right because prior to January 1, 1984 and under Lucas, a contribution of separate property to the acquisition of community property or a single family residences in joint tenancy was considered a gift absent an agreement to the contrary - if a reimbursement was allowed retroactively, then it would negate the gift and impair the vested property right of non-separate property proponent. If this were allowed, the husband in Lucas would have lost one-half the value of the reimbursement.

See generally, In Re Marriage of Buol, 39 Cal.3d 751, 705 P.2d 354, 218 Cal.Rptr. 31 (1985), In Re Marriage of Fabian, 41 Cal.3d 440, 715 P.2d 253, 224
Agreements

The above represents an outline of what is community property and how it applies in a given situation and the ramifications of such.

However, the law allows the parties to have an agreement to alter the effect of the community property laws.

Prenuptial

The first of such agreements are prenuptial and postnuptial agreements.

Prenuptial agreements, if they contain certain essential elements, are favored by the courts. To begin with, such an agreement must be made in contemplation that the marriage relation will continue until the parties are separated by death. Contracts which facilitate divorce or separation by providing for a settlement only in the event of such an occurrence are void as against public policy. In re Marriage of Higgason, 10 Cal.3d 476, 110 Cal.Rptr. 897 (1973).

In 1986, California enacted its version of the uniform act which is now codified in the Family Code at Sections 1601 through 1617.

While any major discussion of prenuptial agreements is beyond the scope of this presentation, it is important to note that case law such as the Marriage of Pendleton & Fireman, 24 Cal. 4th 39, 5 P.3d 839, 99 Cal. Rptr. 2d 278 (2000) and Marriage of Bonds, 24 Cal. 4th 1, 5 P.3d 815, 99 Cal. Rptr. 2d 252 (2000) has had a tremendous impact on the California Act which allows husbands and wives to make a contract regarding almost any aspect of their marriage, except regarding issues of child support. See Family Code Section 1612 (b).

Transmutation Agreements

The next category of agreements are transmutation agreements which are agreements that alter the character of property from either community property to the separate property of one of the spouses or changes the character of separate property of one of the spouses to community property.

Before January 1, 1985, transmutations could be accomplished by a mere oral agreement. The transmutation could be proved by the acts of the parties and their conduct in dealing with the property. No express or formal agreement was required if it could be fairly inferred from all the circumstances and evidence that a community interest was intended by the parties. See In re Nelson's Estate, 224 Cal.App.2d 138, 36 Cal.Rptr. 352 (1964).

Thus, where title was taken in joint names but one spouse wanted to preserve their
separate property interest or wanted to be reimbursed for their separate property contribution, they could prove this with either an oral or written agreement.

Beginning on January 1, 1985, Family Code Section 852 provided that all transmutation agreements must be in writing. Note that January 1, 1985 refers to the date of the transmutation agreement, not the date of the acquisition of the property.

Section 852(a) requires that the transmutation "must be made in writing by an express declaration" that is consented to by the spouse whose interest is affected.

Thus, no oral transmutations are allowed after 12/31/1984.

So just what must the writing contain to be an express declaration?

The case of Estate of MacDonald, 51 Cal.3d 262, 272 Cal.Rptr. 153, (1990) gives us some guidance:

In this case we are asked to decide what type of writing is necessary to satisfy the statute's requirements. In our view, section 5110.730 (a) must be construed to preclude reference to extrinsic evidence in the proof of transmutations. Accordingly, we conclude a writing is not an "express declaration" for the purposes of section 5110.730 (a) unless it contains language which expressly states that a change in the characterization or ownership of the property is being made. At page 266.

What about personal property that has no written title such as jewelry or rugs or paintings?

Family Code Section 852 (c) provides:

(c) This section does not apply to a gift between the spouses of clothing, wearing apparel, jewelry, or other tangible articles of a personal nature that is used solely or principally by the spouse to whom the gift is made and that is not substantial in value taking into account the circumstances of the marriage.

Thus, as long as the value of a gift to the spouse is of an insubstantial value and is of a personal nature, no writing is required to transmute the character from community property to separate property or vice versa. If, however, the value of the item is deemed substantial, then the donor may be able to bring it back into the community property pot if there is no MacDonald writing accompanying the gift.


Additionally, a transmutation of assets for estate planning purposes is a transmutation of assets for dissolution proposes also, even if the transmutation agreement specifically provides that it only applies on death. In Re Marriage of Holtemann, 166 Cal.App.4th 1166, 83 Cal.Rptr.3d 385 (2008).
Commingled Accounts

Tracing

When both separate and community funds have been deposited into a single account, it is said that the account has been commingled.

And upon divorce or death, one spouse is trying to trace to their separate property in order to get some money back.

There are certain concepts that are used to aid in tracing to the source of funds in the account to characterize such funds:

1. The Family Expense Exhaustion Presumption is a general overall concept that is applied to the tracing methods and has two components:

   a. Where there is a commingled account, it is presumed that available community funds have been used first for community expenses and that separate property funds have been used for family expenses only when the community funds have been exhausted. Thus, even though there are numerous deposits into a single account comprising separate and community property, the community property is deemed spent first on family expenses and then the separate property is deemed spent.

   b. When separate property funds are used to pay for family expenses, there is no right to reimbursement unless there is an agreement to that affect between the spouses.

Family expenses should be differentiated from acquisitions. Family expenses are those that are usually thought of as consumption items such as food, vacations, rent and medical care. They do not represent any property that can be divided upon divorce. The basis for the above rules lies in the marital duty of mutual support. Even if there are no community funds, the mutual duty of support still applies and each spouse must use their separate property to discharge this duty. See v. See, 64 Cal.2d 778, 415 P.2d 776, 51 Cal.Rptr. 888 (1966).

The above rules help in splitting out the monies that are in the commingled account. However, what if once the family expense rubric is addressed, there still remains some community property and some separate property in the account and then an asset is purchased? Now what do we do?

When an asset is purchased with funds from a commingled account, there are methods that have been formulated to trace the source of the funds used to make the acquisition.

If the property was UNTITLED OR TITLED only in the name of one spouse, then the General Community Property Presumption applies and it can be rebutted by tracing. The first tracing method is called the Family Expense Exhaustion Presumption mentioned above.
However, note that if an asset is purchased with funds from the commingled account and the separate property proponent wants to use the family expense exhaustion method to show that the funds used to acquire the asset were separate property, if there are community funds and separate funds in the account because the community expenses did not exhaust the community funds, then the purchase would be apportioned between the separate property and the community property.

The other method that can be used by the separate property proponent is the DIRECT TRACING METHOD.

In the case of In Re Marriage of Mix, 14 Cal.3d 604, 536 P.2d 479, 122 Cal.Rptr. 79 (1975) the court noted at page 612:

The first method involves direct tracing... Whether separate funds so deposited continue to be on deposit when a withdrawal is made from such a bank account for the purpose of purchasing specific property, and whether the intention of the drawer is to withdraw such funds therefrom, are questions of fact for determination by the trial court.

Thus, if the separate property proponent uses the direct tracing method and has the requisite intent, then he will prevail in his rebuttal of the General Community Property Presumption. The direct tracing method tends to favor the separate property proponent but detailed records that show each and every deposit and expenditure is necessary and oral testimony may not be enough to show the intent.

Note that when there is community and separate property remaining in an account when an asset is acquired, the direct tracing method is the only way the separate property proponent can trace back to his separate property.

Multiple Party Bank Accounts - Probate Code 5305

In general, joint bank accounts between married persons are presumed to be community property as specifically stated in Probate Code Section 5305:

Section 5305. Married parties; community property; presumption; rebuttal; change of survivorship right, beneficiary, or payee by will.

(a) Notwithstanding Sections 5301 to 5303, inclusive, if parties to an account are married to each other, whether or not they are so described in the deposit agreement, their net contribution to the account is presumed to be and remain their community property.

(b) Notwithstanding Sections 2581 and 2640 of the Family Code, the presumption established by this section is a presumption affecting the burden of proof and may be rebutted by proof of either of the following:

(1) The sums on deposit that are claimed to be separate property can be traced from separate property unless it is proved that the married persons made a written agreement that expressed their
clear intent that the sums be their community property.

(2) The married persons made a written agreement, separate from the deposit agreement, that expressly provided that the sums on deposit, claimed not to be community property, were not to be community property.

(c) Except as provided in Section 5307, a right of survivorship arising from the express terms of the account or under Section 5302, a beneficiary designation in a Totten trust account, or a P.O.D. payee designation, may not be changed by will.

(d) Except as provided in subdivisions (b) and (c), a multiple-party account created with community property funds does not in any way alter community property rights.

Thus, keep in mind that tracing still applies but note that if an asset is acquired in joint names, then to rebut, you must have a writing or statement in the title document stating that it is not community property. If you can show the agreement, you can rebut the community property presumption. If you can not show the agreement, then the asset is community property subject to a right of reimbursement if you can trace to a separate property source.

Thus, with a joint account and the joint acquisition of property, there are two levels of analysis: (1) can you rebut the joint name presumption and (2) can you trace back to the origin of the funds before they were deposited into the joint account.

If the General Community Property Presumption applies because the acquisition is untitled or in one spouse’s name only, can you trace back to the separate property source using the direct tracing or the exhaustion method?

Note again that Family Code Section 2581 and 2640 do not apply to the account - the General Community Property Presumption applies to the account and tracing to the source of funds is the way to rebut.

**Businesses Brought Into the Marriage**

The next area to discuss regarding characterization is a business that one spouse BRINGS INTO the marriage, i.e., it is a separate property business because it was started before the spouse got married, but that spouse continues to work in the business.

Thus, we have two components of the business, the separate property component and secondly, as all efforts during the marriage create community property, there also exists a community property element to the business as well.

Two competing formulas have been developed to measure this bifurcation in characterization:
The **PEREIRA** formula which says that personal efforts are responsible for the rise in value of the business so the separate property component is given a reasonable return on the investment. Ths formula appears to favor the community. *Pereira v. Pereira*, 156 Cal. 1, 103 P. 488 (1909).

The **VAN CAMP** formula says that it is mainly the business itself that created the rise in value and thus, the owner spouse is given a reasonable salary to compensate him/her for their community efforts and the reminder of the value is the separate property of the spouse. This formula appears to favor the separate property proponent. *Van Camp v. Van Camp*, 53 Cal. App. 17, 199 P. 885 (1921).

**How to Characterize Acquisitions on Credit**

Look to the intent of the Lender - Primary or sole reliance

In *Gudelj v. Gudelj*, 41 Cal.2d 202, 259 P.2d 656 (1953), the court, at page 210, stated:

> There is a rebuttable presumption that property acquired on credit during marriage is community property. But "funds procured by the hypothecation of separate property of a spouse are separate property of that spouse." The proceeds of a loan made on the credit of separate property are governed by the same rule. In accordance with this general principle, the character of property acquired by a sale upon credit is determined according to the intent of the seller to rely upon the separate property of the purchaser or upon a community asset. In the absence of evidence tending to prove that the seller PRIMARILY relied upon the purchaser's separate property in extending credit, the trial court must find in accordance with the presumption. Citations omitted, emphasis added.

However, the court in *Marriage of Grinius*, 166 Cal.App.3d 1179, 212 Cal. Rptr. 803 (1985) took a different approach:

> Loan proceeds acquired during marriage are presumptively community property; however, this presumption may be overcome by showing the lender intended to rely SOLELY upon a spouse's separate property and did in fact do so. Without satisfactory evidence of the lender's intent, the general presumption prevails. At page 1187.

Thus, where debt is used to acquire property, look to the intent of the lender to determine how to characterize the debt as either separate property debt or community debt.

**Apportionment of Real Property - Moore/Marsden**

What happens if you bought the house before marriage, took out a loan using your own credit and then got married and you and your spouse use community property to pay off the loan?

2640 does not apply to a community property contribution to the acquisition of separate property - 2640 applies to a separate property contribution to the acquisition of
community property.

This issue was addressed in the early 1980’s and is well summarized by the court in In re Marriage of Nelson, 139 Cal.App.4th 1546, 44 Cal.Rptr.3d 52 (2006) at page 1553 (note that the formulas are a function of the purchase price, not the fair market values at trial):

Generally, "[w]hen community property is used to reduce the principal balance of a mortgage on one spouse's separate property, the community acquires a pro tanto interest in the property. [Citations.] This well-established principle is known as 'the Moore/Marsden rule.' In re Marriage of Moore, (1980) 28 Cal.3d 366, 168 Cal.Rptr. 662, 618 P.2d 208 (Moore ); In re Marriage of Marsden, (1982) 130 Cal.App.3d 426, 181 Cal.Rptr. 910.

In essence, in order to determine the respective interests of the separate property proponent and the community, the first calculation would be to take the separate property contributions that reduce principal divided by the purchase price and the community property contributions that reduce principal divided by the purchase price. Once that ratio is determined for each part, that ratio is then multiplied by the appreciation to determine the share of each in the increase in value.

Once those numbers are determined, then they are added to the respective separate property contributions and the community property contributions to determine what each player receives.

And, under Marsden, the separate property proponent is entitled to all of the pre-marriage appreciation in the house.

Note that unlike 2640, the community here actually receives a pro rata interest in the property.

Improvements - Community Improves Separate, Separate Improves Community

Assuming that our married couple owns a house, either as the separate property of one spouse or as community property, how do we deal with the following:

1. One spouse uses community property to improve their own separate property.

2. One spouse uses their separate property to make improvements to the other spouse's separate property.

3. One spouse uses community property to improve the other spouse's separate property.

The results of using SEPARATE PROPERTY comes either in the form of a gift to the community or to the other spouse prior to January 1, 1984 or, it gives rise to a right of reimbursement - it does not create an ownership interest in the property to which the contribution was made.
Now, the new rule as set out under Family Code Section 2640 allows the separate property proponent to be reimbursed for contributions to improve the community property and for contributions to improve the other spouse’s separate property on a dollar for dollar basis.

Thus, separate to community or separate to separate receives a reimbursement for improvements.

Note under Lucas, above, prior to 1984, a separate property contribution to the acquisition of a community asset was a gift to the community absent an agreement to the contrary.

Now, what about a transfer of community property to separate property for an improvement?

We have seen that a transfer for an acquisition earns the community a pro rata ownership interest in the property under the Moore/Marsden rule. In Marriage of Wolfe, 91 Cal.App.4th 962, 110 Cal.Rptr.2d 921 (2001), the court stated at page 972: 

The application of community funds results in what amounts to co-ownership of the asset (Moore, supra, 28 Cal.3d at pp 371-372, 373-374; Branco, supra, 47 Cal.App.4th at p 1627.) There is no reason to presume a gift when funds are applied to improve separate property. The proper measure of the community’s reimbursement rights is another issue. Although there is no reason to distinguish between improvements and purchases in applying a gift presumption, there is nonetheless a distinction between the two enterprises. The expenditure of community funds to reduce an encumbrance on or otherwise assist in the purchase of separate property necessarily provides a benefit to the record owner measurable upon dissolution of the community. On the other hand, improvements do not always enhance the value of an asset; indeed, ill-advised improvements may well diminish the value of property...On the facts before us, Joyce is at least entitled to one-half of the amount expended on the improvement. At page 973.

In Marriage of Allen, 96 Cal.App.4th 497, 116 Cal.Rptr.2d 887 (2002), the court stated: Where community funds are used to make capital improvements to a spouse’s separate real property, the community is entitled to reimbursement or a pro tanto interest under the Moore/Marsden rule both because its rationale applies equally to the reduction of an encumbrance and to capital improvements. At page 501.

**Life Insurance**

As a general rule, the life insurance policy and the proceeds of the policy if the policy was purchased with community funds or was earned as part of an employment package given during marriage is community property. If community property and separate property are used to acquire the policy, then the proceeds are apportioned pro rata according to the contributions of each to the payment of premiums. When dealing with whole life policies, the cash surrender value is the asset that is being
divided and the characterization of the policy and the proceeds follows the payment of the premiums.

Term policies do not have any cash surrender value and thus, the courts usually look to who paid the premiums for the last term in order to characterize the proceeds. However, in a dissolution action, the appellate courts have not been in agreement. The questions that have been presented are (1) with a policy whose term expires after the period when community funds were used to purchase the policy, is it in fact a divisible asset (2) is a right of renewal a divisible asset and (3) what is the impact on (1) and (2) if the insured is no longer insurable.

Note, However, that the California Supreme Court granted a petition for review in Marriage of Valli (review granted Aug. 24, 2011, S193990; superseded opinion at 195 CA4th 776, 124 CR3d 726) where in a now depublished opinion, the court of appeal held that a life insurance policy purchased during marriage (with pre-separation premiums paid from community funds) listing the wife as sole owner with her husband's consent was her separate property.

On May 15, 2014, the California Supreme Court reversed (58 Cal.4th 1396) and held that purchases made during the marriage are not exempt from the transmutation requirements for converting community property to separate property and that a life insurance policy bought with community assets was community property.

Military insurance benefits are not divisible community assets because federal law pre-empts state law and allows the serviceman complete control over his policy.

**Pensions at Death**

In Boggs v. Boggs, 520 U.S. 833, 117 S. Ct. 1754, 138 L.Ed. 2d 45 (1997), the United States Supreme Court rules that ERISA pre-empted state law regarding qualified plans and as such, overrode Louisiana's community property laws. Thus, the non-participant spouse of the beneficiary of an ERISA qualified plan has no testamentary rights of disposition over her community property interest in the husband's plan.

Thus, one would be under the impression that the estate of the non-participant spouse would not include any of the qualified plan benefits on an estate tax return. However, the following comment is contained in California Civil Practice and Probate Proceedings, Section 17.17, CCPPROBATE Section 17.17:

> Despite the holdings in Boggs and the other cases, an analysis of the exclusions for pension benefits enacted prior to 1986 leads to the conclusion that a one-half community property interest is includible under 26 U.S.C.A. Sections 2033 or 2039. In each instance, a separate exclusion was enacted for the community property interest of the nonparticipant spouse, an indication that he or she had ownership rights that were reportable as a part of the gross estate. [See Section 17:15; Randolph B. Godshall and Michael J. Jones, Updates on Planning for Retirement Benefits after Boggs, 21st Annual Fall Program, Est Planning, Trust and Probate Law Section of State Bar of California, pp. 13-14] Further, it is not clear whether Boggs is applicable to IRAs and other interest arrangements that
are not subject to ERISA. The interests actually includible in the estates of the participant and nonparticipant spouse would have no impact on the tax liability. Since any interests would necessarily pass to the surviving spouse, they would qualify for the marital deduction under 26 U.S.C.A. Section 2056. Though the includibility of qualified plan benefits may have no impact on the federal estate tax, it may affect elections under 26 U.S.C.A. Sections 303, 2032A, 2057 and 6166.

Employee Benefits

As additional forms of compensation, companies have given employees benefits such as termination pay, severance pay and non-qualified deferred compensation.

In re the Marriage of LEHMAN, 18 Cal.4th 169, 955 P.2d 451, 74 Cal.Rptr.2d 825 (1998) at page 180:

Hence, if the right to retirement benefits accrues, in some part, during marriage before separation, it is a community asset and is therefore owned by the community in which the nonemployee spouse as well as the employee spouse owns an interest.

Stock Options

In re Marriage of Hug, 154 Cal.App.3d 780, 201 Cal.Rptr. 676 (1984), the court stated at page 783:

It was not an abuse of discretion, under the facts of this case, for the trial court to allocate those interests by applying a time rule, finding that the number of options determined to be community property is a product of a fraction in which the numerator is the period in months between the commencement of the spouse’s employment by the employer and the date of separation of the parties, and the denominator is the period in months between commencement of employment and the date when each option is first exercisable, multiplied by the number of shares which can be purchased on the date the option is first exercisable. The remaining options are the separate property of the employee.

Gifts

Family Code Section 1100(B) provides that a spouse can not give away community personal property without the written consent of the other spouse.

If the nonconsenting spouse objects, then he or she can sue the donee and recover all of the property for the benefit of the community. If the donor has died, then the nonconsenting spouse can void up to one-half of the gift.

Family Code Section 1100(c) provides that a spouse may not sell the community personal property used as the family dwelling or the furniture in the home or the wearing apparel of the other spouse or minor children without written consent.
Management of Community Owned Business

Family Code Section 1100(d) allows the spouse who is operating a business to have the primary management and control but has to give prior written notice to the other spouse of any sale, lease, exchange, encumbrance or other disposition of substantially all of the business assets.

If a spouse violates this requirement, the remedies are strictly limited to those contained in Family Code Section 1101(g) which include an award of an amount equal to 50% of the value of the asset transferred, plus attorneys fees and if fraud is found under Civil Code Section 3294, the court can award 100 % to the nonoffending spouse.

Fiduciary Duty

Family Code Section 721(b) imposes the duty of highest good faith by the spouses in their dealings with each other.

Debts

Family Code Section 910 provides that the community is liable for a debt incurred by either spouse either before or during the marriage regardless of who has the management and control, and regardless of which spouse is a party to the debt or to a judgment for the debt.

There is no liability for debt under Family Code Section 910 after separation.

Family Code Section 911 provides that earnings of a married spouse during marriage are not liable for a debt incurred by the other spouse before marriage. They continue to not be liable if deposited into a separate account where the other spouse can not withdraw from it and are uncommingled with other community property.

This allows a spouse to put their post marriage earnings into a separate account and not be liable for debts of the other spouse incurred before marriage.

Family Code Section 912 provides that quasi-community property is liable for debts to the same extent as community property.

Family Code Section 913 provides that the separate property of a married person is liable for their own debts incurred either before or after marriage but that spouse's own separate property is not liable for debts of the other spouse, regardless of whether those debts were incurred before or after marriage.

Family Code Section 914 provides that a person is personally liable (including their separate property) for their spouse's debts incurred for the necessaries of life incurred while living together.

Family Code Section 915 provides that a child support obligation that does not arise out of the marriage is treated as a debt incurred before marriage. And if community property is used to pay the support obligation when that spouse has nonexempt
separate income, the community is entitled to reimbursement from that separate property.

**Death**

At the first juncture, it is very important to note that Family Code Section 2581 and 2640 apply only to dissolutions, not to cases involving death. Thus, the joint name presumption and rights to reimbursement for separate property contribution to the acquisition of community property do not apply.

**THUS, AT DEATH, THE PRESUMPTION Follows TITLE.**

It is important to be aware of those title rules above because they apply at death in order to characterize the asset and understand the competing claims.

If we have an intestacy, community property and joint tenancy is treated the same for succession purposes - the surviving spouse receives the community property under Probate Code Section 100 and 6401 and the surviving tenant (i.e., the surviving spouse) receives the joint tenancy by survivorship.

But, if the decedent had a will, he/she could dispose of one-half of the community property to any one they chose but the will would not affect the joint tenancy property which passes automatically to the surviving tenant.

Thus, since the way title is held creates the presumption of an agreement that the parties intended the results that follow title, you can not rebut title by tracing - the title "agreement" must be rebutted by another "agreement".

In **Estate of Blair**, 199 Cal.App.3d 161, 244 Cal.Rptr. 627 (1988), the court stated at page 167:

> For purposes of determining the character of real property on the death of one spouse, there is a presumption that the property is as described in the deed and the burden is on the party who seeks to rebut the presumption.

If the property was acquired before 1985 and they had an agreement that the property was owned other than in joint names, title could be rebutted by either an oral or written agreement - remember that prior to 1985, transmutations could be oral. If the property was acquired after 1984, then title could only be rebutted by a written transmutation agreement.

Thus if the heirs can show an oral or written agreement before 1985 or a written agreement after 1985, they can rebut title; otherwise, the title controls.

On the other hand, if title is in one spouse's name alone or it is untitled property, if acquired during marriage, then you can rebut title by tracing to the source of funds. There is no agreement as to how title is held.

On death, PC 6122 says all provisions in a will are revoked upon dissolution. This
applies to dissolutions after 1984.

Automatic Temporary Restraining Order (ATRO)

The summons and complaint in a dissolution contains the automatic temporary restraining order (ATRO) which prevents each party from transferring or changing the title to any property unless they get consent from the other party or a court order.

However, under subparagraph (b), certain actions are allowed and it is recommended that careful consideration be given to each of the permitted actions, especially where the parties want to make sure that if one of them dies before the court rules on the status of the marriage, that their interest in property is not transferred in a manner that they would not want otherwise, such as survivorship on deeds or dispositions under a revocable trust.

The ATRO must be adhered to in the following circumstances:

Family Code Section 2040. Temporary restraining order; contents; notice; definitions

(a) In addition to the contents required by Section 412.20 of the Code of Civil Procedure, the summons shall contain a temporary restraining order:

(1) Restraining both parties from removing the minor child or children of the parties, if any, from the state without the prior written consent of the other party or an order of the court.

(2) Restraining both parties from transferring, encumbering, hypothecating, concealing, or in any way disposing of any property, real or personal, whether community, quasi-community, or separate, without the written consent of the other party or an order of the court, except in the usual course of business or for the necessities of life, and requiring each party to notify the other party of any proposed extraordinary expenditures at least five business days before incurring those expenditures and to account to the court for all extraordinary expenditures made after service of the summons on that party.

Notwithstanding the foregoing, nothing in the restraining order shall preclude a party from using community property, quasi-community property, or the party's own separate property to pay reasonable attorney's fees and costs in order to retain legal counsel in the proceeding. A party who uses community property or quasi-community property to pay his or her attorney's retainer for fees and costs under this provision shall account to the community for the use of the property. A party who uses other property that is subsequently determined to be the separate property of the other party to pay his or her attorney's retainer for fees and costs under this provision shall account to the other party for the use of the property.
(3) Restraining both parties from cashing, borrowing against, canceling, transferring, disposing of, or changing the beneficiaries of any insurance or other coverage, including life, health, automobile, and disability, held for the benefit of the parties and their child or children for whom support may be ordered.

(4) Restraining both parties from creating a nonprobate transfer or modifying a nonprobate transfer in a manner that affects the disposition of property subject to the transfer, without the written consent of the other party or an order of the court.

(b) Nothing in this section restrains any of the following:

(1) Creation, modification, or revocation of a will.

(2) Revocation of a nonprobate transfer, including a revocable trust, pursuant to the instrument, provided that notice of the change is filed and served on the other party before the change takes effect.

(3) Elimination of a right of survivorship to property, provided that notice of the change is filed and served on the other party before the change takes effect.

(4) Creation of an unfunded revocable or irrevocable trust.

(5) Execution and filing of a disclaimer pursuant to Part 8 (commencing with Section 260) of Division 2 of the Probate Code.

(c) In all actions filed on and after January 1, 1995, the summons shall contain the following notice:

"WARNING: California law provides that, for purposes of division of property upon dissolution of marriage or legal separation, property acquired by the parties during marriage in joint form is presumed to be community property. If either party to this action should die before the jointly held community property is divided, the language of how title is held in the deed (i.e., joint tenancy, tenants in common, or community property) will be controlling and not the community property presumption. You should consult your attorney if you want the community property presumption to be written into the recorded title to the property."

(d) For the purposes of this section:

(1) "Nonprobate transfer" means an instrument, other than a will, that makes a transfer of property on death, including a revocable trust, pay on death account in a financial institution, Totten trust, transfer on death registration of personal property, or other instrument of a type described in Section 5000 of the Probate Code.
(2) "Nonprobate transfer" does not include a provision for the transfer of property on death in an insurance policy or other coverage held for the benefit of the parties and their child or children for whom support may be ordered, to the extent that the provision is subject to paragraph (3) of subdivision (a).

(e) The restraining order included in the summons shall include descriptions of the notices required by paragraphs (2) and (3) of subdivision (b).