

PASS Answer to ESSAY QUESTION 6

[This sample answer was drafted by PASS founders and faculty members Sara Berman-Barrett, Steven Bracci and Bruce Landau —creators of the PASS Bar Review course and PASS the Performance Test On-line. To learn more about PASS, the PASS faculty, and the PASS Bar Review courses, go to www.passlaw.com, or call (310) 288-4374.]

California (“CA”) is a community property (“CP”) state, and, under the laws of the state of California, Henry’s and Wanda’s interests in the property in question will be distributed as follows.

1. The Lake Cabin

The cabin is located in CA, and was acquired while the couple was domiciled in CA, but it was inherited by Wanda (“W”) and therefore would initially be characterized as separate property (“SP”). Property acquired during marriage is generally presumed to be CP, however property obtained by gift, devise or descent is deemed SP, even if obtained during marriage.

W, however, did take some action with respect to the cabin —namely executing the new deed—which may alter the initial characterization.

Transmutation

In 1993, at Henry’s urging, title to the cabin was changed to joint tenancy per the deed. Henry (“H”) will claim that W’s actions of executing the new deed effected a transmutation on the part of W of her SP property to CP. The problem with this argument is that the spouse adversely affected, here W, must consent and accept the transmutation. The facts state that W believed the *only effect* of the conveyance would be to avoid probate. Accordingly, W would argue that by her actions she did *not* intend to transmute and thus did not truly consent to a transmutation; rather she only intended to indicate how she wished that the property be distributed upon her death. If W is successful and the transmutation argument fails, the cabin would remain W’s SP. Because she did, however, at H’s urging, change the title on the deed —making a clear, express written change of the characterization of the property, knowing that the change would have some legal effect, the court may hold W accountable for the change, and allow the attendant benefit to the community.

Title Presumption

If H's transmutation argument is successful, and W's executing and recording the new deed conveying title to H and W as *joint tenants* did change the character of the cabin, H would argue that at divorce, the cabin should be considered CP and accordingly divided 50% each to H and W. H would make this argument based on the CA law that at divorce, property which is held in *any* joint form, such as the joint tenancy here, is *presumed* to be CP.

CA law permits rebuttal of this presumption only with either a clear statement in the deed or other title instrument that the property is SP, or with a written agreement between the parties affirming that the property is SP. Neither of these rebuttal arguments would be available to W: the deed now clearly indicates title held in joint form, and there are no facts indicating any written agreement between the spouses.

Thus, W's best defenses to H's title presumption claim remain to argue, as discussed above, that W was mistaken in the effect of executing the deed, and she did not desire to or consent to a present transmutation; or, to argue as discussed below, that given circumstances of her executing the deed it would be unfair and inequitable to now consider the cabin CP.

Equitable Arguments

In addition to disputing H's transmutation argument, W's might also make the argument, based in equity, that H breached his fiduciary duties to W by falsely informing her of the consequences of the title change, that she detrimentally relied on his assertion that the only effect of the title change would be to avoid probate, and that H should not now benefit from his wrongdoing. W would testify that she agreed to change the deed solely as an estate planning strategy (as evidenced by the fact that the impetus to make the change was the How to Avoid Probate book), and that she did not intend there to be any inter vivos changes. There are no facts, however, to indicate that this was anything other than a mistake on W's part, i.e. no evidence of fraud or coercion on H's part, therefore it does not appear likely that W's equitable arguments will prevail over the clear language of the deed and CA's codified title presumptions.

If the transmutation argument fails, W will receive 100% of the interest in the cabin as SP, but if the H's transmutation argument is successful, H and W will likely each be awarded a 50% interest in the cabin based on the CP title presumption.

2. The Painting

W inherited the painting, thus the painting was initially W's SP. The painting increased in value from \$5,000 to \$50,000, but not because of any time or effort on W's part—simply due to the popularity of the artist. As a general rule, productive property creates additional proceeds of the same character, absent action on the part of the owner spouse to change the initial characterization. Here, W does not appear to have taken any actions intending to change the painting's SP character, and thus, similar to a productive stock portfolio or other productive property that increases in value, W would likely be awarded 100% of the painting at its full \$50,000 value.

Note that if H were successful in the transmutation argument with respect to the cabin (see above), and if, as such, the cabin were deemed CP, H might make the argument that when W hung her SP painting in the CP cabin, it became *affixed* to the real property and thus took on the character of that real property. It seems unlikely that H would prevail with such an argument, however, both because it is unclear whether the transmutation argument will succeed (and if it fails the cabin remains W's SP), and because, even if the cabin were CP, merely hanging a painting on the wall does not appear to be sufficient action to effectively transform the character of the painting itself.

3. The State X House

At dissolution, property acquired during marriage while the spouses are domiciled outside CA is deemed quasi-community property ("QCP") if it would have been considered CP under CA law had the spouses been domiciled in CA when the property was acquired. At divorce, QCP is generally divided just as is CP, 50% to each spouse.

Characterization of residence under CA law

To address the initial issue of how the house would be characterized under CA law, we must first note that it was purchased during marriage, and property acquired during marriage is generally CP.

Downpayment and Mortgage

Second, the initial sources, both the downpayment and the balance, would also likely have been deemed CP in nature under CA law.

The downpayment came from the couple's savings (which appear to be from earnings during

marriage (CP) since they were married while still students) and thus, the downpayment portion would have been characterized as CP.

The balance was *purchased on credit* with a twenty-year mortgage. Credit purchases are characterized at the time the loan is obtained, based on the *intent of the lender* test. The facts do not indicate who signed the mortgage note, nor is there much evidence of what monies the lender would have been looking to for repayment of the loan. However, when they purchased the home, W was a stay-at-home mother and H was the sole breadwinner. Given this, and given the fact that subsequent mortgage payments were paid from Henry's earnings (which in CA would be CP), it is likely that the lender was looking to H's earnings to repay the mortgage, and that therefore the loan portion would also initially have been characterized as CP (under CA law.)

Transmutation

Next, however, H will try to argue that because title to the State X house was in H's name alone, the property was transmuted from its initial status as CP to H's SP. The facts do not state the year that title was placed in H's name alone. In fact, we don't know date of the house purchase; we only learn from the facts that it was between 1980 and 1990.

The CA rules regarding transmutations changed during that time period. Simply registering title as SP does not turn a CP asset into an SP asset. As of January 1, 1985, transmutations in CA have had to be in writing (which writing must clearly evidence the intent to transmute). Further, under this current law, the spouse adversely affected must consent to the transmutation. Here, that would be W, and there is no evidence that consented to titled being in H's name alone, (or, for that matter even that W knew how title was taken). Thus, if the deed in question were written after January 1, 1985, H's transmutation argument would fail.

If however, the deed were executed before December 31, 1984, H might try to argue that the deed evidenced a fully executed *oral* transmutation agreement between the spouses. Prior to January 1, 1985, transmutation agreements were permissible where oral and implied, so long as they were fully executed. The court may accept such an argument, especially if W has no evidence with which to rebut the oral transmutation argument. In such a situation, the contest would become a "he said/ she said" testimony/credibility battle, and there are no facts to indicate whether W or H is likely to be more credible to the court.

Distribution of the Interests in the Value of the House

If the court accepts the oral transmutation argument, H would be awarded a 100% interest in the State X house. Even if the court refuses H's oral transmutation argument, however, H would

nominally be awarded 100% of the interest in the State X house; whether or not the house were considered CP under CA law, the CA courts do not have jurisdiction to divide real property in another state. Therefore, the CA divorce court would have to achieve the desired community outcome by awarding W 50% of the *value* in the State X house as an offset. (Note the CA court could accomplish this either by awarding W other property equal to 50% of the State X house's value, perhaps by giving her more of some other CP asset such as the podiatry practice, or by ordering that H "buy out" W's 50% share of the value of the State X house.)

4. Wanda's professional education and podiatry practice

Education/Professional Degree

Where the community finances the obtaining of a professional degree by one of the spouses during marriage, the resulting increase in earning power has been held to be a CP asset, and thus the community is generally entitled to be reimbursed for contributions to tuition, books and the like. Here the facts do state that Wanda obtained a degree in podiatry after three years of study paid for out of Henry's earnings, and therefore it would initially appear that the community should be reimbursed for these expenses.

This right to reimbursement, however, may be reduced or even eliminated by factors such as where the community has already received a substantial benefit or where the need for support to which that spouse (here W) would otherwise be entitled to has been reduced or eliminated.

Note that there is a presumption that where the education occurs less than ten years before the dissolution, the community has not received such a substantial benefit. However, that presumption is not conclusive. Here, to rebut the presumption, W would argue that before obtaining her degree she was not working outside the home and thus her obtaining the degree reduced or perhaps even eliminated support payments that she would have otherwise been entitled to receive.

Further, the facts specifically state W's practice became "quite successful" because of her "enthusiasm, skill, and willingness to work long hours," and, therefore, W would argue, in those seven years following her obtaining the degree she worked as hard as an ordinary person would have worked in ten years, and that the community was more than adequately compensated for the expense of obtaining the degree by the revenue that her successful practice brought into the community during those seven years. If the court accepts W's arguments, as seems likely here, there would be little or no reimbursement to the community for W's educational expenses.

Podiatry practice

The value of the practice, including any hard assets (such as medical equipment, furniture, etc.),

accounts receivable (monies due on services rendered), along with the goodwill value of the practice (often thought of as the expectation of continued public patronage), will all be considered CP assets under CA law, and as such, each spouse will have a 50% interest in the full value of the podiatry practice at the time nearest separation.