

PLANNING WITH THE FAILED MARRIAGE IN MIND

OR

WHERE IS MY PROPERTY?

DALLAS ESTATE PLANNING COUNCIL

January 5, 2006

**CLASSIFICATION OF MARITAL PROPERTY
IN TEXAS**

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1. General. In order to advise clients in Texas with respect to their property, there must be a clear understanding of the classification, ownership, management and claims that can be asserted against their property. Texas has what is known as the community system of property rights of husband and wife. All marital property is either separate or community. All property owned by the spouses during the marriage is presumed to be community property. The spouse who wishes to claim separate property status has the burden of showing, by clear and convincing evidence, that the property is separate.
2. The Constitution. It is the Texas Constitution which ultimately defines what is separate or community property and not the legislature or the parties involved. *Arnold v. Leonard*, 114 Tex. 535, 273 S.W. 799 (1925). Article XVI § 15 of the Texas Constitution provides that all property, both real and personal, of a spouse owned or claimed before marriage, and that acquired afterward by gift, devise or descent, shall be the separate property of that spouse; provided, that persons about to marry and spouses, without the intention to defraud pre-existing creditors, may by written instrument from time to time partition between themselves all or part of their property, then existing or to be acquired, or exchange between themselves the community interest of one spouse or future spouse, in any property for the community interest of the other spouse or future spouse and other community property then existing or to be acquired, whereupon the portion or interest set aside to each spouse shall be and constitute a part of the separate property and estate of such spouse or future spouse. Spouses may also from time to time, by written instrument, agree between themselves that the income or property from all or part of the separate property then owned or which thereafter might be acquired by only one of them shall be the separate property of that spouse, with gifts of property from one spouse to the other presumed to include all of the income or property which might arise from that gift property. Spouses may also agree in writing that all or part of the separate property owned by either or both of them shall be the spouses' community property.

3. Characterization.

- a. Separate Property. Separate property of a spouse is that property, real or personal, owned or claimed before marriage, and that acquired afterward by gift, devise or descent and certain recovery for personal injuries (other than for loss of earnings capacity). Tex. Fam. Code § 3.001. It also includes separate property which has been created by a “partition” (or division) of the married couple’s community property. Separate property also includes property acquired with that party’s separate property.
- b. Community Property. There is no definition of community property. If an asset does not fall within the constitutional definition of separate property, it must be community property – the “Rule of Implied Exclusion” remains the true test of what is community property. In other words, community property is that property of the marriage which is not proven to be separate property. Community property is further divided into different categories depending upon the management rights, including:
 - i. Sole Management Community Property.
 - (1) Earnings from a spouse.
 - (2) Income from a spouse’s separate property.
 - (3) The increases and mutations of and the revenues from that spouse’s sole management property.
 - ii. Joint Management Community Property.
 - (1) Sole management property that is mixed with sole management property of the other spouse.
 - (2) All other community property.
 - iii. Quasi Community Property.
 - (1) Separate property of a spouse which was acquired while the spouses were not residing in Texas but that would have been community if they had resided in Texas at the time of acquisition is treated in divorce proceedings as if it were community property. Tex. Fam. Code § 7.002.
 - (2) Such property is treated as separate if the marriage terminates by reason of a spouse’s death. *Hanau v. Hanau*, 730 S.W.2d 663 (Tex. 1987).

4. Management of Marital Property.

- a. Separate Property. Each spouse has sole management, control and disposition of his/her separate property. Tex. Fam. Code § 3.101.
- b. Special Community Property. Each spouse has sole management, control and disposition of the community property he/she would own, if single, including personal earnings, revenue from separate property, recoveries for personal injuries and increases in revenues from his/her “special community property.” Tex. Fam. Code § 3.102(a).
- c. Joint Community Property. All other community property is subject to both spouse’s joint management, control and disposition – the “joint community property.” Tex. Fam. Code § 3.102(b).

5. Special Classification of Property.

- a. Divorce. Upon the divorce of the spouses, a family court can divide the community estate in a manner that is just and right. The community estate includes the sole management community property of both spouses, the joint management and the quasi community property estate.
- b. Separate Property. The family court cannot divest a spouse of that spouse’s separate property in divorce proceedings.

6. Marital Property Liability.

- a. Statutory Plan. The Legislature’s rules of marital property liability are found in § 3.202 and § 3.203 of the Texas Family Code.
 - i. Separate Property Exemption. A spouse’s separate property is not subject to the liabilities of the other spouse. Tex. Fam. Code § 3.202(a).
 - ii. Special Community Exemption. A spouse’s special community property is not subject to the liabilities incurred by the other spouse prior to the marriage or any non-tortuous liabilities of the other spouse incurred during the marriage. Tex. Fam. Code § 3.202(b).
 - iii. Other Rules. The above exemptions exist unless both spouses are personally liable under “other rules of law.” Tex. Fam. Code § 3.202(a) and (b).
- b. Debtor’s Spouse’s Property. A debtor’s spouse’s separate property and special community property and a spouse’s joint community property are subject to any

liabilities that spouse incurred before or during the marriage. In addition, the special community estates of both spouses are subject to the tortious liabilities of either spouse incurred during the marriage. Tex. Fam. Code § 3.202(c) and (d).

- c. Community Presumption. Notwithstanding the significance of the substantive rules of characterization, the importance of the community presumption cannot be ignored. Generally, all assets of the spouses on hand during the marriage and upon its termination are presumed to be community property thereby placing the burden of proof on the party (a spouse or that spouse's personal representative) asserting separate character to show by "clear and convincing evidence" that a particular asset is in fact separate. Tex. Fam. Code § 3.003.
 - i. Tracing. The community presumption prescribed by Tex. Fam. Code § 3.003 requires the party asserting that a particular asset is separate to prove the facts that justify such legal conclusion by "clear and convincing evidence." This burden is met by tracing an existing asset through its mutations to its original separate property source. This requires records of assets, acquisitions, sales, purchases and other transactions and history of segregated separate property, bank accounts.
 - ii. Co-mingling. If separate property assets cannot be identified through tracing, then the asset will be presumed to be community property through co-mingling and lose their separate identity.
- d. Community Out First Rule. Commentators have expressed an opinion that where community funds and separate funds are deposited into a single account and there is an absence of contemporaneous records accounting for the separate and community funds thereafter expended, it is generally presumed that community funds are first withdrawn, whether the withdrawals are used for the support and maintenance of the family or for the purchase of property. In other words, mixing community funds with separate funds is like mixing oil and water with community property being oil which rises to the top. Disbursements from the account are presumed to be first made from the community. Funds remaining in the account remain separate to the extent the account balance never drops below the amount of separate funds deposited. Accordingly, it is important to maintain the separate account balance to the extent of separate property originally contributed to the account to avoid co-mingling. Property purchased from a separate property account which includes community is presumed to be purchased from the community funds based upon the "first out" rule.

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