

Overview of Characterization & Tracing in a Divorce

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I. BASIC PREMISE OF CHARACTERIZATION

The essential question in every divorce involving any amount of property involves a determination of which marital estate owns the property: the community estate, husband's separate estate, wife's separate estate, or a combination of two or more of these estates. The rules of characterization define the answer, although the solution may not be easy or clear.

A. Community Property Presumption

1. Community Property Defined

Community property consists of the property, other than separate property, acquired by either spouse during the marriage. Tex. Fam. Code § 3.002. Property possessed by either spouse during or on dissolution of marriage is presumed to be community property. Tex. Fam. Code §3.003(a). Money borrowed on a community obligation is community property. Similarly property acquired on the credit of the community is community property. *Gleich v. Bongio*, 99 S.W.2d 881, 883. (Tex. 1937).

2. Separate Property Defined

Separate property consists of property owned before the marriage, or acquired through devise (death with a will) or descent (death without a will). An item of property is also separate in nature if it is a gift to a spouse. Where spouses partition or exchange their property between them in a written agreement, like a premarital or postmarital agreement, the property will be separate. An increase in the value of an item of separate property is an inherent part of the item and cannot be separate from it. *Lipsev v. Lipsey*, 983 S.W.2d 345, 350 (Tex. App. – Fort Worth 1998, no pet.)

Recovery for personal injuries sustained during the marriage, including disfigurement and past and future pain and suffering, is the separate property of the injured spouse. Tex. Fam. Code §3.001(3).

However, any recovery for lost earnings, lost earning capacity, and/or medical and other expenses remains community property. *Graham v. Franco*, 488 S.W.2d 390, 396 (Tex. 1972).

A gift is a transfer of property made voluntarily and gratuitously. *Parkhurst v. Weiting & Tucker*, 850 S.W.2d 726, 730 (Tex. App. – Corpus Christi 1993, writ denied). A gift requires (1) an intent to make a gift at the time of conveyance; (2) unconditional delivery of the property; and (3) acceptance of the property. *Id.*; *Ellebracht v. Ellebracht*, 735 S.W.2d 658, 659 (Tex. App. – Austin 1987, no writ). Lack of consideration is an essential characteristic of a gift such that an exchange of consideration precludes a gift. *Parkhurst*, 850 S.W.2d at 730.

A conveyance from a parent to a child is presumptively a gift. *Ellebracht*, 735 S.W.2d at 659. Any property labeled as a "gift to the community" is the undivided separate property of each spouse; each spouse owns an undivided one-half interest in the property. *In re Marriage of Royal*, 107 S.W.3d 846, 851 (Tex. App. – Amarillo 2003, no pet.).

When separate property is used to acquire property during marriage and title is taken in the names of both spouses, the spouse who contributed the separate property is presumed to have made a gift of half of the separate funds to the other spouse unless rebutted by evidence clearly establishing that there was no intent to make a gift. *Cockerham v. Cockerham*, 527 S.W.2d 162, 168 (Tex. 1975).

3. Mixed Character

Property can be owned by more than one marital estate. Purchases made partly with separate and partly with community funds will be community property to the extent and in the proportion that the consideration is furnished by the community, with the spouse supplying the separate funds having an interest in the property to the amount of his or her investment. The whole property is held as tenancy in common between the respective estates.

B. Inception of Title Doctrine

The inception of title rule provides that a property takes its status as separate or community property at the time of its acquisition. Its character is fixed at that time. *Henry S. Miller Co. v. Evans*, 452 S.W.2d 426, 430 (Tex. 1970). Inception of title occurs when a party first has a right of claim to the property by virtue of which title is finally vested. *Saldana v. Saldana*, 791 S.W.2d 316, 319 (Tex. App. – Corpus Christi 1990, no writ). It is the origin of the title to property and not the

acquisition of final title that determines the property's character. *Jensen v. Jensen*, 665 S.W.2d 107, 109 (Tex. 1984).

C. Rebutting the Community Property Presumption

To overcome the community property presumption, the person asserting a separate property claim must show by clear and convincing evidence that the property is separate in character. Tex. Fam. Code §3.003(b). To rebut the presumption, a spouse must generally trace and clearly identify property claimed as separate property. *McElwee v. McElwee*, 911 S.W.2d 182, 188 (Tex. App. – Houston [1st Dist.] 1995, writ denied). If the evidence shows that the community property and separate property have been so comingled as to defy resegregation and identification, the burden is not discharged and the statutory presumption prevails. *Id.*

The character of separate property is not changed by the sale, mutation, exchange, substitution, or change in the form of separate property. *Gleich*, 99 S.W.2d at 881. If separate property can be definitely and accurately traced and identified, it remains separate property regardless of the fact that the separate property undergoes mutations or changes in form.

1. Tracing Generally

Tracing involves establishing the separate origin of the property through evidence showing the time and means by which the spouse originally obtained possession of the property. *Hilliard v. Hilliard*, 725 S.W.2d 722, 723 (Tex. App. – Dallas 1985, no writ). Separate property will retain its character through a series of exchanges so long as the party asserting separate property ownership can overcome the presumption of community property by tracing the assets on hand during the marriage back to property that, because of its time and manner of acquisition, is separate in character. *Cockerham*, 527 S.W.2d at 168.

In essence, the characterization of the asset is shown by a paper trail beginning at the time of the acquisition of the asset and continuing to the date of divorce, which trace clearly shows that the property is separate property based upon the date of inception of title and/or the characterization of the funds used to purchase the asset. *Ganesan v. Vallabhaneni*, 96 S.W.3d 345, 354 (Tex. App. – Austin 2002, pet. denied). At the end of any attempted tracing, any doubt as to the character of the property should be resolved in favor of the community estate. *Akin v. Akin*, 649 S.W.2d 700, 703 (Tex. App. – Fort Worth 1983, writ ref'd n.r.e.).

The most common reasons for tracing are:

1. To establish the separate character of funds or assets held on account during marriage;
2. To establish the separate character of an asset acquired during marriage from separate funds or assets;
3. To support an economic contribution claim by demonstrating the use of funds or assets of one marital estate to benefit or enhance another marital estate;
4. To defeat an economic contribution claim from one marital estate to another by demonstrating that the benefit or enhancement was paid by the estate receiving the benefit.

Janice L. Green, Thomas L. Ausley, James D. Stewart, and J. Kenneth Huff, *Characterization and Tracing Workshop*, ch. 34, p. 24, 29th Annual Advanced Family Law Course (2003).

There are six principal rules for tracing and clearly identifying separate property:

1. Clearing house method or identical sum inference.

The clearinghouse method is useful if a party had an account into which separate funds were temporarily deposited and then withdraw. It assumes that one or more identifiable withdrawals were made that are clearly the withdrawals of the separate funds and are therefore separate property themselves. Time can bar the usefulness of this method of tracing.

The identical sum method involves only one deposit followed by an identical withdrawal made within a short time frame.

2. Minimum Sum Balance

The minimum sum balance method is used when you have an account with separate property funds in it, into which community funds are deposited and when there have only been a few identifiable transactions. The party seeking to provide the separate character of the funds traces the account through each transaction to show that the balance of the account never went below the amount proven to be separate property.

3. Community Out First Rule

Under this rule, withdrawals from a mixed separate and community fund are presumed to be community to the extent that community funds exist. Withdrawals are presumed to be from separate funds only when all of the community funds have been exhausted.

4. Pro Rata Approach

If mixed funds are withdrawn from an account, the withdrawal should be pro rata in proportion to the respective balances of separate and community funds in the account. By using this approach, it is not necessary to analyze the character of each withdrawal.

5. Item Tracing

An item of separate property on hand at dissolution of marriage must be traced to its inception of title. The burden is on the party claiming the separate property character.

6. Value Tracing

Value tracing is used to trace cash assets in order to determine the character of cash on hand at the dissolution of marriage. The proponent of separate property must trace all funds brought into and out of an account. Each deposit and each check must be accounted for.

[This is simply an overview of the various methods of tracing. Articles cited at the end of this paper may provide a more exhaustive treatment of the topic.]

2. Burden of Proof

The general rule is that to discharge the burden imposed by the statute, a spouse, or one claiming through a spouse, must trace and clearly identify property claimed as separate property. *Tarver v. Tarver*, 394 S.W.2d 780, 783 (Tex. 1965); *McKinley v. McKinley*, 496 S.W.2d 540, 543 (Tex. 1973).

However, the managing spouse who commingles his interest in property with the property of the other spouse is under the burden to trace his interest, whether community or separate, if he wishes to overcome the presumption that it all belongs to the estate of the other spouse. *Farrow v. Farrow*, 238 S.W.2d 255 (Tex. Civ. App. – Austin 1951, no writ).

The plain wording of the statute creates the rebuttable presumption that all property possessed by a husband and wife upon divorce is community property and imposes the burden upon the one asserting otherwise to prove the contrary by “clear and convincing evidence”. *Tarver*, 394 S.W.2d at 783; *Vallone v. Vallone*, 644 S.W.2d 455 (Tex. 1982).

This standard falls in between the preponderance of the evidence standard in civil proceedings and the beyond a reasonable doubt standard from criminal proceedings. *Thomas v. Thomas*, 277 S.W. 210, 212 (Tex. Civ. App. – Beaumont 1925, writ dismissed). The Texas Pattern Jury Charge defines “clear and

convincing evidence” as “that measure or degree of proof that produces a firm belief or conviction that the allegations sought to be established are true.” While the proof must weigh heavier than merely the greater weight of the credible evidence, there is no requirement that the evidence be unequivocal or undisputed. *Boyd v. Boyd*, 131 S.W.3d 605 (Tex. App. – Fort Worth 2004, no pet.).

The burden of proof is not discharged when evidence shows that separate and community property have been so commingled as to defy resegregation and identification.

a. Appellate Review of Separate Property Characterization

The heightened burden required in proving separate property characterization can be better understood when examined in the context of appellate review standards. A mischaracterization that is of such magnitude that it affects the just and right division of the community estate will result in a remand to the trial court for a just and right division based upon the correct characterization of the property. *Boyd*, 131 S.W.3d at 617.

When an appellate court conducts a legal sufficiency review of a separate or community property finding by the trial court, they look at all the evidence in the light most favorable to the finding to determine whether a reasonable trier of fact could have formed a firm belief or conviction that its finding was true. *In re J.F.C.*, 96 S.W.3d 256, 266 (Tex. 2002). This means that the reviewing court must (1) assume that the fact finder resolved disputed facts in favor of its finding if a reasonable fact finder could do so and (2) disregard all contrary evidence that a reasonable fact finder could have disbelieved or found to have been credible. *Id.* However, the reviewing court is not required to disregard undisputed facts that do not support the finding because that might skew a clear and convincing analysis. *Id.* If the reviewing court determines that no reasonable fact finder could form a firm belief or conviction of the truth of the matter to be proved, then the evidence is legally insufficient. *Id.*

When an appellate court conducts a factual sufficiency review of a separate or community property finding, they consider whether all of the evidence is such that a fact finder could reasonably form a firm belief or conviction about the truth of the allegations sought to be established. *In re C.H.*, 89 S.W.3d 17, 25 (Tex. 2002). The reviewing court considers whether disputed evidence is such that a reasonable fact finder could not have resolved that disputed evidence in favor of its finding. *In re J.F.C.*, 96 S.W.3d at 266. If, in light of the entire record, the disputed evidence that a

reasonable fact finder could not have credited in favor of the finding is so significant that a fact finder could not reasonably have formed a firm belief or conviction, then the evidence is factually insufficient. *Id.*

b. Evidentiary Considerations

The proponent of the tracing should gather every item of evidence possible to satisfy the burden. Usually this includes bank records, deeds, closing statements, earnest money contracts, probate records, tax returns, brokerage statements, etc. Frequently spouses do not maintain such records, so parole evidence is the only proof available. Mere probative evidence may not be sufficient to satisfy the burden of clear and convincing evidence.

The lack of records to support the tracing may not necessarily be fatal. Some courts of appeals, such as Beaumont and Corpus Christi, take a strict view of the needs for records, holding that testimony only was insufficient to support the tracing. *Harris v. Ventura*, 582 S.W.2d 853 (Tex. Civ. App. – Beaumont 1979, no writ); *Jones v. Jones*, 890 S.W.2d 471 (Tex. App. – Corpus Christi 1994, no writ). Other courts of appeals, such as Dallas, Fort Worth, Amarillo, Tyler and Austin, take a more liberal view regarding the lack of evidence, allowing testimonial evidence to support a separate property finding in the absence of documentation. *Holloway v. Holloway*, 671 S.W.2d 51 (Tex. App. – Dallas 1983, writ dismissed); *Newland v. Newland*, 529 S.W.2d 105 (Tex. Civ. App. – Fort Worth 1975, writ dismissed); *Peterson v. Peterson*, 595 S.W.2d 889 (Tex. Civ. App. – Austin 1980, writ dismissed); *Celso v. Celso*, 864 S.W.2d 652 (Tex. App. – Tyler 1993, no writ); *In the Matter of the Marriage of Thurmond*, 888 S.W.2d 269 (Tex. App. – Amarillo 1994, writ denied).

Thus, even though records were not offered into evidence, there was other evidence tending to support the position of the proponent of the trace. A lack of records, coupled with a lack of credible corroborating evidence does not meet the clear and convincing test.

II. THE BIG TEN TEXAS SUPREME COURT DECISIONS

Cheryl Wilson summarized the 10 main cases out of the Texas Supreme Court in her article from the 2004 Advanced Family Law Course. Cheryl L. Wilson, Krystal M. Cordova, *Characterization and Tracing: Follow the Yellow Brick Road*, ch. 5, pp. 6-8, 30th Annual Advanced Family Law Course (2004).

In spite of the hundreds of opinions on the

question of the character of marital property, there are a relatively small number of Supreme Court opinions which form the basis of Texas community property theory. The principles announced in these opinions are the basis for most questions of characterization of marital property. They are presented here in chronological order.

1. *Welder v. Lambert*, 44 S.W. 281 (Tex. 1898) – Inception of Title

In *Welder v. Lambert*, the children of James Power's first marriage and his children by his second marriage sued each other. Power had contracted with the state of Coahuila and Texas for a land grant of 4 ½ leagues of land situated in Refugio County in 1828. He married his first wife in 1832 and they had two children. Title to the property came to him during the first marriage. Thereafter, the first wife died, he married a second time and had five children with that wife. The children of the first marriage claimed that because title was transferred to him during his marriage to their mother, it was the community property of that marriage and that they were entitled to one-half through their rights under their mother and to two-sevenths of the remaining one-half as heirs of the father. The children of the second marriage claimed that it was not community property of either marriage since his right to title incepted prior to either marriage and that the heirs of the first marriage are only entitled to two sevenths of the whole. Because his right to demand title to the property came into being prior to his marriage, the court held that it was his separate property. This opinion was based upon the Spanish concepts of *bienes gananciales*, in which the court noted were included causes of action. The husband had entered into a fixed contract right prior to his first marriage. This entitled him to acquire the land by compliance with the terms of the contract. The court found that this contract right was property under the Spanish law. Within the meaning of 'bienes' was the concept of a chose in action. That is, if a spouse came into the marriage with the right to bring an action (here to force conveyance of title), then it was his separate property. "The title relates to its origin, and must take the impress of its character from it." Hence the beginning of what we now know as the inception of title rule.

2. *Arnold v. Leonard*, 273 S.W. 799 (Tex. 1925) – Constitution Defines Separate Property

There the wife sought injunctive relief to prevent husband's creditor for executing upon the rents and revenues deriving from her separate real property. The Court recited the provisions of Tex. Const. art. XVI, §15: "All property, both real and personal, of the wife, owned or claimed by her before marriage and that

afterward by gift, devise or descent, shall be her separate property; and laws shall be passed more clearly defining the right of the wife, in relation as well to her separate property as that held in common with her husband. Laws shall also be passed providing for the registration of the wife's separate property." The test to determine character is limited by the constitutional definition of separate property. The court held that the legislature had no power to either enlarge or diminish the definition of wife's separate property. The legislative effort to declare rents and revenues from separate property to be separate was invalid. The concept that the legislature has no authority to expand the definition of separate property beyond the constitutional provisions was firmly engrafted upon Texas jurisprudence in the Arnold opinion. Thus began the long history of classifying marital property by the measure of the constitution.

3. *Gleich v. Bongio*, 99 S.W.2d 881 (Tex. 1937)
– Proportional Ownership

In *Gleich v. Bongio*, two lots had been purchased during marriage. The purchase was accomplished by cash payment from husband's separate funds and the remainder by a note carried by the vendor, which was secured by the real property. The court noted that property acquired on the credit of the community is community property. However, where it can be shown that the acquisition is made with part separate and part community, the marital estates own an interest in proportion to the consideration each supplied. "Generally purchases made partly with separate and partly with community funds will be community property to the extent and in the proportion that the consideration is furnished by the community, the spouse supplying the separate funds having a separate interest therein to the amount of his or her investment, the tenure of the whole property in such cases being by way of a sort of tenancy in common between the separate and community estates."

4. *Norris v. Vaughan*, 260 S.W.2d 676 (Tex. 1953) – Mineral Lease Payments Are Separate Property

Prior to marriage, husband had owned a 7/8th determinable fee, as lessee, in seven gas wells, known as the "Pakan Wells." During the marriage, husband had received \$80,661.00 from the gas production. The Court's determination of this issue centered on an analysis of the nature of a mineral lease. A lessee in an oil and gas lease owns a determinable fee in the oil and gas in place, and thus an interest in realty. The lessee's interest will last only so long as oil or gas is produced, and it is a matter of judicial knowledge that oil and gas

producing territory will become exhausted in time. The production and sale of the natural gas in this instance is equivalent to a piecemeal sale of the separate corpus, and funds acquired through a sale of separate corpus, if traced, will remain separate property. Thus the production from the Pakan Wells was held to be husband's separate property. During marriage, husband acquired two other wells, known as the "Hill and Cantrell Wells." Husband used his separate funds to pay for the cost of drilling and to bring the minerals into production. "The principle which lies at the foundation of the whole system of community property is, that whatever is acquired by the joint efforts of the husband and wife, shall be their community property." The use of his separate funds to acquire the title did not change the community character.

5. *Graham v. Franco*, 488 S.W.2d 390 (Tex. 1972) – Separate Property Includes Injuries to the Person

The question of the constitutionality of Tex. Rev. Civ. Stat. 4619 (now codified at Tex. Fam. Code §3.001(3)) was in issue. That statute provided that the "recovery awarded for personal injuries sustained by either spouse during marriage shall be the separate property of that spouse except for any recovery for loss of earning capacity during marriage." The Constitution makes no reference to the separate character of recovery for personal injuries. Here, the Court opined that the question of the character of personal injury recovery lies in whether or not the right to the recovery is "property." The Court noted that at the time the constitution was adopted, there was a large body of law holding that a chose in action for injuries to the person was not regarded as property. Further, at common law, a cause of action for personal injuries was not subject to inheritance or assignment. But even if the cause of action is property, then the right violated is to personal security and no right is more intensely separate than this; and the violator of this separate right gives rise to a separate cause of action. It was also noted that injuries to a wife under the Spanish law were her separate right. For example, "...if her separate property house were set afire and destroyed by a third person, the recovery should be her separate property... If the arm of the wife is cut off, the recovery for the loss because of disfigurement and for the attendant pain and suffering should go to the wife. The reasoning is that the recovery is a replacement...and not the 'acquisition' of an asset by the community estate." Finally, the Court opined that in adopting the provision of Tex. Const. art XVI §15, the people did not intend to change the common law or the Spanish law under which Texas operated so as to make a cause of action for injuries to the wife an asset of the community.

6. *Nail v. Nail*, 486 S.W.2d 761 (Tex. 1972)

In *Nail v. Nail*, the trial court had considered the personal goodwill in establishing a value of the husband's medical practice. The Supreme Court held that the accrued good will was not an earned or vested property right, nor did it qualify as "property subject to division." It did not constitute an asset separate and apart from the person. It would be extinguished in the event of his death, retirement, or disablement. It was not "property within the estate" of the parties. In the thirty years following this opinion, there has not been a reported case which has substantially developed the question which the opinion left open. That is, the Court stated: "It is to be understood that in resolving the question at hand we are not concerned with good will as an asset incident to the sale of a professional practice.." If the proper fact pattern is presented, a court will be required to determine the character of the actual proceeds of a sale. The Nail opinion does not say that the good will is separate property, only that it is property not subject to division. However, if a sale has occurred and funds from the sale are on hand at the time of a divorce, there will be a reckoning of this dilemma.

7. *Cockerham v. Cockerham*, 527 S.W.2d 162 (Tex. 1975). – Debt Incurred During Marriage is Presumed to be on Credit of the Community

Debts contracted during the marriage are presumed to be on the credit of the community and thus are joint community obligations, unless it is shown the creditor agreed to look solely to the separate estate of the contracting spouse for satisfaction. Thus, property acquired on the credit of the community is community property.

8. *Cearley v. Cearley*, 544 S.W.2d 661 (Tex. 1976) – Retirement Benefits do not Follow Inception of Title Rule

The *Cearly* opinion generally stands for the proposition that nonvested retirement benefits are divisible on divorce.

For many years, retirement plans were governed by the companion cases *Taggart v. Taggart*, 522 S.W.2d 422 (Tex. 1977) and *Berry v. Berry*, 647 S.W.2d 945 (Tex. 1983), which instructed on the division of the community portion of defined contribution and defined benefit retirement plans. However, effective September 1, 2005, for all pending or new cases, §3.007 provides a new method of division for such plans.

9. *Eggemeyer v. Eggemeyer*, 554 S.W.2d 137 (Tex. 1977) – Separate Real Property Not Subject to

In *Eggemeyer*, the trial court awarded wife an undivided one-third interest in a small family farm, which husband owned as his separate property. It was held that the trial court's mandate to divide the "estate of the parties" does not include the power to divest a spouse of separately owned real property. The nature of property is fixed by the Constitution, and not by what is "just and right." The only "estate of the parties" is community property. A spouse may not be divested of title to his separate real property.

10. *Cameron v. Cameron*, 641 S.W.2d 210 (Tex. 1982) – Separate Personal Property Not Subject to Division.

Cameron further elaborates on *Eggemeyer*, holding that a spouse's separate personal property is not part of the "estate of the parties" and, therefore, not subject to division.

III. RECENT CASE LAW DEVELOPMENTS

A. Characterization

1. *Russell v. Russell*, 2006 WL 241476 (Tex. App.–Houston [1st Dist] 2006, no pet.) (memorandum op.) (not designated for publication).

The Houston 1st District Court of Appeals held that wife was estopped from challenging her characterization of the property in question as husband's separate property because her sworn inventory satisfied the requirements of a judicial admission. As such, the trial court erred in characterizing the property at issue as community. The party attacking the characterization of the property has the burden of proof to show, by clear and convincing evidence, that the trial court mischaracterized the property. In order to overcome the community presumption, a spouse claiming certain property is separate rather than community must trace and clearly identify the property claimed as separate. Although wife argued that husband cannot rely on her inventory classifying the property at issue as husband's separate property in order to meet the clear and convincing standard because it was not admitted into evidence, the Court noted that the inventory constituted a judicial admission. Judicial admissions estop a party from challenging their truth. Here, the conditions that must be met before a party's admission is conclusive against her were established with regard to the property at issue: (1) wife clearly designated the property at issue as husband's separate property; (2) the trial court had the inventory before it during trial and referred to it during trial; (3) the inventory was deliberately made, clear and unequivocal as to wife's characterization; (4)

wife's counsel relied on the inventory in eliciting testimony from husband and wife; and (5) at no time did wife challenge the accuracy of the inventory. Further, wife explicitly admitted that one of the items was husband's separate property when she testified at trial as to how the trial court should make a just and right division of the estate.

2. *Prague v. Prague*, 190 S.W.3d 31 (Tex. App.—Dallas 2005, pet. denied).

The Dallas Court of Appeals held that the evidence was sufficient to support the trial court's findings that a portion of wife's teachers Retirement System (TRS) account were wife's separate property, the benefits available at the time of retirement for TRS were not totally generated during the marriage, and that a portion of the TRS benefits was owned by wife before marriage. When the Court reviews an alleged property characterization error in a divorce proceeding, the Court must determine not only whether the trial court's finding is supported by clear and convincing evidence, but also whether the characterization error, if established, caused the trial court to abuse its discretion. To overcome the community presumption, the spouse claiming certain property as separate property must clearly identify the property claimed to be separate. Whether marital property is separate or community is determined by inception of title, which occurs when a party first has the right of claim to the property. Marital property that is characterized as separate property does not change, although the property might be improved with community funds. Here, the Court held that the evidence was sufficient to support the trial court's finding that monies borrowed from wife's TRS benefits were paid for the reinstatement of TRS during a time when the parties were separated, and that the reinstatement payment came from wife's separate property. The Court also held that the Taggart formula, rather than the Berry formula, applied to determine the value of the community and separate property portions of TRS benefits. Further, testimony of wife's expert was sufficient to support the valuation of wife's TRS benefits where his testimony specifically delineated values for the separate property and community portions of the benefits, was based upon the same valuation tables and discount rates used by TRS, and reflected the nine years worked by wife prior to the marriage as separate property.

3. *Sooy v. Sooy*, 2007 WL 516259 (Tex. App.—San Antonio 2007, no pet. h.) (not designated for publication).

The San Antonio Court of Appeals held that because husband's Impairment Income Benefit is compensation for his injuries suffered from a work-

related accident and not compensation for his lost wages, it is his separate property. A spouse's personal injury damages that are not characterized as recovery for "loss of earning capacity during marriage," are the claimant spouse's separate property. Any workers' compensation payment intended to replace earnings lost during a claimant spouse's marriage is community property. Tex. Fam. Code 3.008(b). Additionally, any workers' compensation a spouse receives is "characterized in the same manner as the income being replaced," regardless of when the claim was filed.

4. *McSweeney v. McSweeney*, 2007 WL 247677 (Tex. App.—San Antonio 2007, no pet. h.) (not designated for publication).

The San Antonio Court of Appeals held that husband's disability payments pursuant to his retirement plan from the postal service were for civil service disability retirement and were thus community property and subject to division in a divorce action. The Court of Appeals also held that wife was entitled to one-half of husband's civil service disability retirement payments in the divorce action, even though husband and wife were married 11 of the 16 years he worked for the postal service prior to becoming disabled, husband left wife, failed to pay his child support obligation under the temporary orders, husband was employed and wife was not, and wife would have continued to benefit from payments had the marriage continued.

B. Tracing

1. *Mock v. Mock*, 216 S.W.3d 370 (Tex. App.—Eastland 2006, pet. denied)

The Eastland Court of Appeals held that wife failed to rebut presumption of community property with respect to funds in savings account held in her name. At trial, wife testified that her father gave her yearly gifts of \$10,000.00 in the form of checks but did not testify as to how many of the gift checks she deposited in her savings account or for how many years she received them. Wife produced no records. The Court noted that a party seeking to rebut the community presumption with respect to property acquired during marriage must trace the assets on hand during marriage back to property that, because of its time and manner of acquisition, is separate in character. Tex. Fam. Code 3.003(a). Tracing of separate property for the purposes of rebutting the community property presumption involves establishing the separate origin of the property through evidence showing the time and means by which the spouse originally obtained possession of the property. As a general rule, testimony that funds are separate property without any tracing of the funds is insufficient to rebut

the community presumption. Here, wife's testimony that funds received during the course of marriage were separate property without any tracing was insufficient to rebut the community presumption. As such, the trial court did not err in characterizing the savings account as community property.

2. *In the Matter of the Marriage of Rohling*, 2006 WL 1112825 (Tex. App.—Amarillo 2006, no pet.)(memorandum op.) (not designated for publication)

The Amarillo Court of Appeals held that the trial court erred in characterizing four items as husband's separate property based on his mere testimony that the items were purchased with separate property funds. The Court noted that mere testimony that property was purchased with separate property funds, without a tracing of the funds, is generally insufficient to rebut the community presumption. Here, since husband failed to present any tracing evidence to overcome the community presumption, the trial court could not have formed a firm belief or conviction that the items at issue were husband's separate property. Husband failed to establish by clear and convincing evidence that the items were his separate property. In reviewing an alleged characterization error, the Court must determine whether the trial court's findings are supported by clear and convincing evidence, but also whether the characterization error, is established, constitutes more than a *de minimis* effect. Mere mischaracterization of community property as separate property does not require reversal.

C. Burden of Proof

1. *Brock v. Brock*, 192 S.W.3d 895 (Tex. App.—Dallas 2006, no pet.)

In *Brock*, the Dallas Court of Appeals held that the trial court did not err in characterizing investment accounts and the pre-marriage balance of an IRA as husband's separate property. The Court noted that in order to overcome the community presumption, the spouse claiming certain property as separate property must clearly identify the property claimed as separate. When asked to review an alleged characterization error regarding property in a divorce action, the Court must determine not only whether the trial court's finding of separate property is supported by clear and convincing evidence, but also whether the characterization error, if established, caused the trial court to abuse its discretion.

2. *Cardwell v. Cardwell*, 195 S.W.3d 856 (Tex. App.—Dallas 2006, no pet.)

In *Cardwell v. Cardwell*, the Dallas Court of

Appeals held that husband failed to meet his burden of establishing, by clear and convincing evidence, that a Kansas oil and gas venture was his separate property. The Court noted that neither husband's testimony nor a page produced by husband, listing the Kansas oil and gas venture as an asset, failed to establish how the asset was procured. Husband therefore failed to overcome the community presumption.

3. *Long v. Long*, ___ S.W. 3d ___, 2007 WL 475794 (Tex. App.—El Paso 2007, pet. pending).

The El Paso Court of Appeals held that the evidence established ex-husband gifted an undivided one-half interest in a lake lot to wife. The property at issue in this case was purchased during marriage with husband's separate funds but titled in both husband and wife's names. Husband claimed the lot in its entirety as his separate property. However, wife claimed an undivided one-half interest in the lot as her separate property, asserting that by using his separate funds to purchase the property and taking the title in both parties' names, husband manifested an intent to make a gift. A gift is a voluntary transfer of property to another made gratuitously and without consideration. Three elements are required to make a gift: (1) intent to make a gift; (2) delivery of the property; and (3) acceptance of the property. Without intent, there is no gift. Similarly, the intent must exist at the time of the transfer, not at the time of a subsequent divorce. In factual sufficiency review, the Court gives due consideration to evidence that the fact finder could reasonably have found to be clear and convincing. Where one spouse uses separate funds to purchase property during marriage and takes title to the property in joint names, the Court presumes a gift to the spouse is intended. This presumption can be rebutted by parol evidence and a rebuttable presumption shifts the burden of producing evidence to the party against whom it operates. Once that burden is discharged and evidence contradicting the presumption has been offered, the presumption disappears and is not weighed or treated as evidence.

Here, husband bore the burden to plead and prove by clear and convincing evidence that the lake lot was purchased with separate property. This he did. The deed to the lot created a rebuttable presumption of a gift because it was purchased with his separate property and title was taken in both names. The presumption vanished when husband testified that he did not intend to make a gift. Wife then had the burden to establish, by clear and convincing evidence, that a gift was intended.

A two-prong standard of review applies to alleged characterization errors. The Court must first determine whether the trial court's finding of separate property is supported by clear and convincing evidence, then examine whether the characterization error, if

established, caused the trial court to abuse its discretion. (Showing of error - showing that error was harmful). The Court stated however, that in a singular instance, where wife can establish that Blackacre is her separate property, it is unnecessary to show harm because divestiture of separate property is reversible error. The Court in this case noted that traditional sufficiency review is heightened when the burden of proof is clear and convincing. In legal sufficiency review, when the burden of proof is clear and convincing, the Court looks at all the evidence in the light most favorable to the fact finder to determine whether a reasonable trier of fact could have formed a firm belief or conviction that the finding was true.

4. *Todd v. Todd*, 173 S.W.3d 126 (Tex. App.–Fort Worth 2005, pet. denied).

The Fort Worth Court of Appeals held that the farm was wife's separate property for equitable distribution purposes, and that wife defeated the community presumption with regard to the farm by clear and convincing evidence. Although husband argued that wife failed to overcome the community presumption regarding the farm because she did not refer to the legal description of the farm or offer into evidence documents, such as a deed, showing her legal ownership of the farm; the Court held that wife sufficiently described the location of the farm to identify it when testified that she lived on road 2117, 550, had a farm out there, and there was no evidence admitted at trial concerning any other farm or ranch. The Court stated that all the evidence at trial pointed to the conclusion that wife owned the farm before marriage. Further, during the trial husband never claimed the farm was community property and referred to it multiple times as "her house." As such, the trial court did not abuse its discretion in awarding the farm to wife as her sole and separate property.

IV. RECENT STATUTORY DEVELOPMENTS

A. Retirement Benefits

Retirement benefits, to the extent they derive from employment during the marriage, constitute community property. *Cearly*, 544 S.W.2d at 662. Such benefits are considered to be "a mode of employee compensation earned during a given period of employment." *Id.* Thus, retirement, pension, and annuity benefits earned during the marriage are part of the community estate, while benefits earned before and after the marriage are the employee spouse's separate property. *Id.* The character of the retirement benefits is not governed by the inception of title doctrine. Instead, the benefits are broken down into monthly increments, the characterization of each depending on

when the increment arises – during marriage or before/after. R. Scott Downing, *Property Puzzles: Characterization, Tracing, 25 Rules and More*, ch. 19, p. 12, 31st Annual Advanced Family Law Course (2005).

Effective September 1, 2005, the law pertaining to characterization of retirement benefits changed. Thus, the previous *Berry/Taggart* apportionment formula no longer applies. Instead, characterization and tracing principles derive from §3.007 of the Texas Family Code.

Note: The new statutory characterization scheme applies only when the retirement plan contains both separate and community portions. Where the retirement plan is 100% community, the statute does not apply.

1. Defined Benefit Plans

A spouse who is a participant in a defined benefit retirement plan has a separate property interest in the monthly accrued benefit the spouse had a right to receive on normal retirement age, as defined by the plan, as of the date of marriage, regardless of whether the benefit had vested. Tex. Fam. Code §3.007(a). The community property interest in a defined benefit plan shall be determined as if the spouse began to participate in the plan on the date of marriage and ended that participation on the date of dissolution or termination of the marriage, regardless of whether the benefit had vested. Tex. Fam. Code §3.007(b).

Caveat: The sum of the separate property benefit and the community property benefit calculated under this formula does not equal one-hundred percent of the total accrued benefit. It is not clear how that phantom benefit will be characterized under case law.

2. Defined Contribution Plans

The account balance in the employee's defined contribution plan on the date of marriage is separate property. The increase in the account balance between the date of marriage and date of divorce is community property. *Pelzig v. Berkebile*, 931 S.W.2d 398, 402 (Tex. App. – Corpus Christi 1996, writ ref'd). A portion of the increase in the account balance, however, may be a result of an increase in the value of the investments in the plan that predated the marriage. Increases in the market value of a separate property security during marriage remain separate property. *Bakken v. Bakken*, 503 S.W.2d 315, 318 (Tex. Civ. App. – Dallas 1973, no writ). To avoid this result, the separate property interest of a spouse in a defined contribution retirement plan may be traced using the tracing and characterization principles that apply to a

nonretirement asset. Tex. Fam. Code §3.007(c).

Caveat: The non-employee spouse may be placed in the position of assuming the burden of tracing the employee spouse's separate property interest in order to prove the community interest.

B. Stock Options

If the option or stock was granted to the spouse before marriage but continued employment during marriage was required before the grant could be exercised or the restriction removed, the spouse's separate property interest is equal to the fraction of the option or restricted stock in which:

1. the numerator is the period from the date the option or stock was granted until the date of marriage; and,
2. the denominator is the period from the date the option or stock was granted until the date the grant could be exercised or the restriction removed.

Tex. Fam. Code §3.007(d)(1).

If the option or stock was granted to the spouse during the marriage but required continued employment after marriage before the grant could be exercised or the restriction removed, the spouse's separate property interest is equal to the fraction of the option or restricted stock in which:

3. the numerator is the period from the date of dissolution or termination of the marriage until the date the grant could be exercised or the restriction removed; and,
4. the denominator is the period from the date the option or stock was granted until the date the grant could be exercised or the restriction removed.

Tex. Fam. Code §3.007(d)(2).

The characterization of the marital property interest in an option or restricted stock described above must be recalculated if, after the initial division of the option or stock, the vesting occurs on a date earlier than the vesting date stated in the original grant of the option or stock. This recalculation must adjust for the shortened vesting period and applies to options and stock granted before and during the marriage. Tex. Fam. Code §3.007(e).

V. REFERENCE ARTICLES

This article was intended to be a basic overview of the principles related to characterization and tracing of marital property assets. For a more detailed treatment of the issues, the following articles would be helpful:

5. Christopher K. Wrampelmeier, "Whose Property Is It Anyway?" – *Characterization*, ch. 5, 32nd Annual Advanced Family Law Course (2006).
6. Charla Bradshaw Connor, "Some of that Retirement Stuff is Mine" *The Current State of Qualified Retirement Plans (Defined Benefit & Defined Contribution)*, ch. 12, 32nd Annual Advanced Family Law Course (2006).
7. Heather L. King, *Marital Property 101*, ch. 18, State Bar College "Spring Training" Course (2005).
8. R. Scott Downing, *Property Puzzles: Characterization, Tracing, 25 Rules, and More*, ch. 19, 31st Annual Advanced Family Law Course (2005).
9. Cheryl L. Wilson, *Characterization and Tracing: Follow the Yellow Brick Road*, ch. 5, 30th Annual Advanced Family Law Course (2004).
10. Janice L. Green, Thomas L. Ausley, James D. Stewart, and J. Kenneth Huff, *Characterization & Tracing Workshop*, ch. 34, 29th Annual Advanced Family Law Course (2003).