#D-312 3/25/80

Memorandum 80-28

Subject: Study D-312 - Creditors' Remedies (Liability of Property of Married Persons--Unresolved Issues)

This memorandum presents a number of policy issues not previously resolved by the Commission concerning the liability of marital property for debts. The latest revised version of the draft statute is attached as Exhibit 1 and the draft of conforming changes is attached as Exhibit 2.

Priority of Application of Property

The Commission has adopted the general rule that all of the community property, as well as the spouse's separate property, is liable for the debt of a spouse. The Commission reserved the question whether there should be some order of priority of application of the property to satisfy the debt. For example, if the debt was incurred for community purposes, should the community property be first exhausted before resort to the debtor's separate property is permitted? If the debt was incurred for separate purposes, should the separate property of the debtor be first exhausted before resort to the community property is permitted?

Existing California law prescribes an order of priority in two situations. Civil Code Section 5122(b) requires a determination whether or not a tort judgment arises out of an activity that benefits the community. If the activity was for the benefit of the community, the judgment must be satisfied first out of community property and then out of the separate property of the tortfeasor; if the activity was not for the benefit of the community, the judgment must be satisfied first out of the separate property of the tortfeasor and then out of community property.

> 5122. . . .
> (b) The liability of a married person for death or injury to person or property shall be satisfied as follows:
> (1) If the liability of the married person is based upon an act or omission which occurred while the married person was performing an activity for the benefit of the community, the liability shall first be satisfied from the community property and second from the separate property of the married person.
> (2) If the liability of the married person is not based upon an act or omission which occurred while the married person was performing an activity for the benefit of the community, the liability shall first be satisfied from the separate property of the married person and second from the community property.

This provision represents a compromise among three conflicting policies evidenced in the treatment of liability of marital property for torts in other community property jurisdictions. These policies are: (1) Community debt principle--the community is an entity that should be liable only for those activities intended to enhance it. (2) Adequacy principle--giving injured persons access to an adequate fund for compensation. (3) Ownership principle--make property of tortfeasor liable only to extent of tortfeasor's interest in property. See generally discussion in Note, Tort Debts Versus Contract Debts: Liability of the Community Under California's New Community Property Law, 26 Hastings L.J. 1575 (1975). No matter how sound the policies that support this provision, it presents grave procedural problems in its operation. These problems are examined below.

The other situation under existing California law where a priority of application of property is required is where separate property of a nondebtor spouse is liable for necessaries of the debtor spouse. Under Section 5132 of the Civil Code, the separate property of a nondebtor spouse liable for the support of the debtor spouse if the community property is first exhausted:

> 5123. A spouse must support the other spouse while they are living together out of the separate property of the spouse when there is no community or quasi-community property.
>
> For the purposes of this section, the terms "quasi-community property" and "separate property" have the meanings given those terms by Sections 4803 and 4804.

This scheme appears to make sense from a policy viewpoint. The separate property of a nondebtor spouse should be liable for debts pursuant to the support obligation of the spouses only where there are no community funds or separate funds of the debtor available for support.

The problem with such schemes is making them work. When a creditor levies on the separate property of a nondebtor spouse, how is it to be proved that the community property and the separate property of the debtor spouse has been exhausted?

The judgment creditor could be required to make an affidavit at the time of levy to the effect that there is no other property available. The nondebtor spouse could controvert the affidavit by offering up any

community property under his or her management and control; in such a case, the debtor spouse should have the opportunity to make exemption claims for the property. But what about community property not under the management and control of the nondebtor spouse (e.g., a business managed by the debtor spouse), and what about separate property of the debtor spouse? If the nondebtor spouse points out some that may be available, is the judgment creditor first required to go after that property? Suppose there is a possibility or even a probability that the property may be exempt? Or suppose that to realize on the asset will require special court orders and receivers, with extensive costs, for an asset of small value?

These questions raise the basic issue, how does a priority scheme work in practice? The staff has been able to find nothing illustrating the operation of the priority provisions. A Note in the Hastings Law Journal speculates on the operation of the priorities provision relating to tort debts:

> With regard to tort debts, on the other hand, such spouse might be able to defeat a levy on particular community property by citing the mandatory priority scheme in Section 5122 and demonstrating that the separate property of the debtor-spouse is sufficient. Conceivably, the required proof could be made in a procedure similar to that set out in section 689 of the Code of Civil Procedure, which provides a way in which third persons claiming an interest in property which has been levied upon can assert their claims. [Note, Tort Versus Contract Debts: Liability of the Community Under California's New Community Property Law, 26 Hastings L.J. 1575, 1596 (1975).]

The staff has also examined the law of other community property jurisdictions for guidance. Texas, Arizona, and Nevada have rudimentary statutes imposing a priority in some instances that offer little guidance; Washington apparently is in the same position by judicial decisions. New Mexico has a more elaborate statutory scheme that creates a presumption of community debts and requires an order of priority of property in satisfying the debts; if property is levied upon out of order, an exemption must be claimed for the property or the order of priority is waived. There is no experience yet under the New Mexico statute, and one of the drafters of the statute speculates that supplementary proceedings may be necessary to ascertain the character of the property for priority purposes. Bingaman, The Community Property Act of

1973: A Commentary and Quasi-Legislative History, 5 N.M. L. Rev. 1 (1974).

Professor Reppy offers a possible solution to the procedural problem:

> A creditor needs statutory assurance that his levy of execution will not be upset under section 5122 after it has been accomplished. Therefore, the statutory scheme should invite the creditor to give notice to the spouse of the tortfeasor (the tortfeasor himself as a party to the tort suit is well aware that a levy of execution is imminent) that he or she has so many days to file with the creditor a list of properties claimed to be primarily and secondarily liable under section 5122. (Any hearing held in court would controvert the accuracy of the priority list.) If no action were taken by the notified spouse, a levy of execution conducted after the specified period of time would be immune from an attack based on section 5122. Until a statutory procedure is enacted the spouse seeking to invoke section 5122 apparently must utilize whatever equitable procedures are generally appropriate to restrain a levy of execution. (I am unaware of any existing basis for shifting the costs of such a proceeding to the tortfeasor when it is initiated by his spouse.)

The problems the staff has with this solution are that it places too much of a burden on the nondebtor spouse in case of errors or omissions, it requires the nondebtor spouse to speculate what separate property of the debtor spouse may be available, and it may require additional court proceedings. Moreover, there are difficulties where there is a change in assets after compilation of the list, and again the question whether in order to exhaust the list the creditor must first levy on assets that appear may be exempt or may be more costly to reach than they are worth.

The staff believes the mechanical problems in imposing an order of priority of application of the property are too great to justify such a provision, no matter how theoretically sound it may appear. The creditor should be able to reach any property available to satisfy the judgment; a priority scheme can best be implemented as between the spouses by means of reimbursement provisions, if that is felt necessary.

Reimbursement

If a nondebtor spouse's separate property is seized for a debt for necessaries of the debtor spouse, should the nondebtor spouse be entitled to reimbursement out of the community property or the separate property of the debtor spouse? If a debt incurred for the benefit of

the community is satisfied in whole or part from the separate property of the debtor, should the debtor spouse be entitled to reimbursement from the community or from the separate property of the nondebtor spouse on a pro rata basis? If a debt incurred for the separate benefit of the debtor spouse is satisfied in whole or part out of community property, should the community be entitled to reimbursement from the debtor spouse?

Under existing law, debts are classified as community or separate at the time of dissolution of marriage for purposes of dividing the assets and liabilities of the community. If during marriage a spouse satisfies a community debt out of the spouse's separate property, the spouse is not entitled to reimbursement at dissolution. See, e.g., See v. See, 64 Cal.2d 778, 415 P.2d 776, 51 Cal. Rptr. 888 (1966). If following separation and before dissolution of the marriage, a spouse satisfies a community debt out of the spouse's separate property, the spouse is entitled to reimbursement at dissolution unless the satisfaction was pursuant to the spouse's support obligation. See, e.g., In re Marriage of Epstein, 24 Cal.3d 76, 592 P.2d 1165, 154 Cal. Rptr. 413 (1979). If during marriage a spouse satisfies a separate debt out of community property, the community is entitled to reimbursement at dissolution. See, e.g., Weinberg v. Weinberg, 67 Cal.2d 557, 432 P.2d 709, 63 Cal. Rptr. 13 (1967). If following separation and before dissolution of the marriage a spouse satisfies a separate debt out of community property, the law is not clear whether the community is entitled to reimbursement, although following the reasoning of Epstein, it probably would be.

Professor Reppy's general position is that in all these situations, where property of one type is seized to satisfy a debt of another type, reimbursement is appropriate and the reimbursement right should be codified and strengthened by statute. He also suggests that the reimbursement right should be immediate and should not be required to await dissolution of marriage. The staff has serious reservations about these suggestions; they appear to foster interspousal litigation without any real purpose. In any event, they are matters more appropriately considered in the context of our general community property--equal management and control--division of property study. It is unnecessary to

resolve these issues for purposes of drafting our creditors' remedies statute.

Liability for Debts Incurred After Separation

As a general rule, the separate property of a debtor spouse and the community property is liable for debts incurred during marriage. Should there be a different rule for debts incurred during marriage at a time when the spouses are living separate and apart?

Under existing law, there is no distinction between debts incurred before or after separation. While it might be argued that a debt incurred after separation will ordinarily be the separate debt of the debtor spouse for which only the separate property should be liable, this is not necessarily true. A debt incurred after separation may easily be for the community benefit, such as for improvements to community property. Moreover, a rule that immunizes the community property from the debts of a spouse incurred after separation would operate unduly harshly on creditors, who may extend credit unaware of the separation. The staff agrees that existing law is sound applying the same rules to liability of property for debts incurred before or after separation.

Where there is a legal separation and division of the property, the property of each spouse should be liable for the debts of that spouse, whether incurred before or after the legal separation. Section 5120.050 (liability of property after division) is drafted to include rules of liability after a division of property pursuant to a legal separation. See discussion of that section, infra.

There is one area where the separation of the spouses may make a difference. Under existing law, the separate property of a nondebtor spouse is liable for debts for necessaries incurred by the other spouse while they are living together pursuant to the obligation of mutual support. Civil Code § 5132. If the spouses have separated by agreement, however, the separate property is not liable unless support is also required by the agreement. Civil Code § 5131. Professor Reppy argues for the repeal of this provision--"One who marries another undertakes a support obligation that cannot be waived by contract antenuptially nor during marriage and cohabitation; at separation waiver is now

allowed. I believe the necessaries doctrine must apply to separated spouses, for this reason, absent the permitted waiver." Professor Bruch takes the same position in Bruch, The Legal Import of Informed Marital Separations: A Survey of California Law and A Call For Change, 65 Calif. L. Rev. 1015, 1030-31 (1977). The staff agrees; the separate property of the nondebtor spouse should be liable for necessaries so long as the spouses are married unless support is waived at separation. However, the necessaries for which the nondebtor spouse is liable after separation should be only the common necessaries of life; the nondebtor should not be required to maintain the estranged spouse in the accustomed life style. See Section 5120.030. Whether there should be an order of priority for application of the property (e.g., first the property of the debtor spouse, then the property of the community, then the property of the nondebtor spouse), and whether the nondebtor spouse should have a right of reimbursement, are separate questions which are dealt with above.

§ 5120.040. Liability of property after interspousal transfer

Transmutation of property from community to separate and from separate to community between the spouses can affect the liability of the property for debts of the spouses. The general rule is that if a transfer is not fraudulent as to creditors of the transferor, the transfer can affect the right of creditors to reach the property.

Whether a transfer is fraudulent as to creditors is determined by the Uniform Fraudulent Conveyance Act, which is found at Civil Code Sections 3439-3440. Under the Uniform Act, a conveyance is any transfer of nonexempt property. Section 3439.01. The following conveyances are fraudulent:

(1) A conveyance that is made without fair consideration and that renders the transferor insolvent is fraudulent as to creditors (without regard to the actual intent of the transferor). Section 3439.04.

(2) A conveyance that is made without fair consideration and that reduces the capital of the transferor to an unreasonably small amount for a business or transaction is fraudulent as to creditors and as to persons who become creditors during the business or transaction (without regard to the actual intent of the transferor). Section 3439.05.

(3) A conveyance made without fair consideration when the transferor intends to incur debts beyond his or her ability to pay as they mature is fraudulent as to both present and future creditors. Section 3439.06.

(4) A conveyance made with actual intent to hinder, delay, or defraud creditors is fraudulent as to both present and future creditors.

The staff believes this set of rules is sound and is appropriate for interspousal transfers. Existing law appears to apply the Uniform Act to interspousal transfers, but there are no good cases precisely on the point on transmutation between community and separate property under the Act. Section 5120.040 makes clear that the Uniform Act applies to interspousal transfers.

A distinct question is whether there should be any formalities required before a transfer is recognized as a valid transfer, either between spouses or to affect the rights of creditors. This is a practical problem since a creditor who levies upon property in anticipation of satisfying a judgment may be unexpectedly faced with a claim that a transmutation has been made, thereby removing the property from the creditor's reach. The potential for fraud in this situation is obvious and real.

In California, the cases are quite liberal in permitting transmutation of property by spouses and require few formalities; a showing of subjective intent and some objective evidence is all that is required. A transmutation of real property may even be by oral agreement, despite the fact there is no exception for this in the statute of frauds. Needless to say, the rules relating to transmutation have been roundly critized by the commentators. See, e.g., 7 B. Witkin, Summary of California Law Community Property § 73 (8th ed. 1974).

One reason for the liberality of the case law is that it has developed primarily in the context of interspousal litigation over property division at dissolution of marriage. For purposes of interspousal property rights, the doctrine of gifts and a policy of mutual or unilateral understanding is predominant.

The staff believes that some formalities such as a recorded writing should be required if a transmutation is to affect the rights of creditors to reach the property. Such formalities would eliminate fraud on

creditors by spouses suddenly claiming at the time of execution that they had an oral agreement transmuting the character of the property. Recordation would give constructive, and perhaps actual, notice to creditors who extend credit that some property may not be available to satisfy a judgment. And a recorded writing would substantially reduce litigation over the character of assets sought to be applied to satisfaction of a judgment. Whether the same or other formalities should be required to affect the rights of the spouses as between each other is a question the staff believes should be deferred until the Commission takes up its general community property study.

A number of other community property jurisdictions require some formalities before a transmutation of the character of property will affect the rights of creditors to reach the property. A detailed analysis of the law of transmutation in the other community property jurisdictions, prepared for the staff by a Stanford law student, is attached as Exhibit 3. Arizona requires that a gift of real property be evidenced by a conveyance and proof of intention to convey. In Idaho, a transmutation of community real property to separate property must be made by an acknowledged deed to be effective. Louisiana requires that a marital contract changing the character of property be signed and acknowledged by the spouses and, in order to affect third-party rights, recorded in the county in which real property is located and in the county where the spouses reside for personal property. New Mexico requires either a written transmutation or clear and convincing proof that a transmutation has been made. An agreement to convert community to separate property must be in writing in Nevada and cannot affect rights of creditors. A transmutation in Texas must be by a conveyance in writing signed by both spouses; a conveyance of real property does not affect BFPs unless the conveyance is acknowledged and recorded. A transmutation of community real property to separate property in Washington requires a deed signed, sealed, executed, and acknowledged by the grantor.

Professor Reppy, in the sole trader study, proposes that if a transmutation of property is to affect the rights of creditors, it should be by a writing that is recorded with the county recorder. The

staff agrees with this proposal and has drafted Section 5120.040 accordingly.

One common means of transmutation of property during marriage is by a premarital contract that affects property acquired during marriage. Such a marriage settlement contract must be executed and acknowledged or proved in the same manner as a grant of land, and must be recorded with the recorder of each county in which real estate affected by the contract is situated. Civil Code §§ 5134-5135. Professor Reppy thinks the recordation provision should either be repealed or amended to indicate that recordation is also necessary to bind third-party creditors where personal property is at issue and is transmuted under an antenuptial contract. See Exhibit 4. The staff believes amendment is preferable--a creditor should have notice that personal as well as real property may be unavailable to satisfy a judgment. The conforming changes (Exhibit 2) include the suggested amendment to Section 5135, although the staff has drafted the amendment more broadly to require recordation for all purposes, not just for purposes of binding creditors.

Joint Tenancy Property Acquired With Community Funds

A matter related to but distinct from transmutation of community property into joint tenancy is whether property, the deed to which indicates it is held in joint tenancy, is in fact joint tenancy or is really community property. This problem arises frequently where community funds are used to acquire property by a deed made out to the spouses as "joint tenants." Whether the property is in fact joint tenancy depends upon the intention of the parties.

Professor Reppy suggests a number of approaches that could be taken to supply more certainty to the law: (1) Conclusive presumption that property acquired during marriage with community funds is community unless the instrument contains a statement signed by both spouses that the property is taken as joint tenancy. (2) Recognition of a new category of property--community property with right of survivorship--and creation of a presumption that property taken as joint tenants is community with right of survivorship unless negated on the face of the title instrument. (3) Recognition of community property with right of survivorship, with no requirements as to the wording of the deed.

The rationale of the last two suggestions is the theory that people take property in joint tenancy primarily for the survivorship benefits; creation of a survivorship right in community property would decrease use of the joint tenancy among spouses. The staff believes there is substantial merit to each of the suggestions. The Commission should decide which approach, if any, it wishes to take.

§ 5120.050. Liability of property after division

Suppose one spouse incurs a debt during marriage but, before the creditor seeks to collect the debt, the spouses are separated or divorced and the property divided. Before the separation or divorce, the creditor could reach the separate property of the debtor spouse and all the community property. After the separation or divorce, there is no community property for the creditor to reach, only separate property. Can the creditor go after property in the hands of the nondebtor spouse on the ground that it was formerly community property and, therefore, should remain liable for the debts?

Under existing law, the rights of creditors are not affected by division of community assets and obligations. The cases have held that a creditor can reach former community property awarded to the nondebtor spouse even though the division of property by the court or by agreement of the spouses may require that the debtor spouse pay the debt. In such a situation, if the property awarded to the nondebtor spouse is seized to satisfy the debt, the nondebtor spouse has a cause of action against the debtor spouse for reimbursement.

Professor Reppy has a number of suggestions for legislative clarification of the law relating to the action by the judgment creditor (making nondebtor spouse a party, permitting nondebtor spouse to assert defenses of debtor spouse, specifying what property is subject to execution), as well as to the action between the former spouses for reimbursement (availability of interest, attorney's fees, and litigation expenses for the nondebtor spouse). However, after considering the improvement of the existing system proposed by Professor Reppy, the staff is of the opinion that the whole scheme is wrong and should be changed.

Why set off a chain reaction, with the creditor going against one former spouse and then that former spouse going against the other? It is a system that breeds litigation. We permit the creditor to reach the community property during marriage because, under one view of the relevant policy, any other system of partitioning the property during an ongoing marriage is disruptive and impractical to administer; after the creditor reaches community assets, the spouses are left to readjust their rights as between each other. But where there has already been a separation or divorce and a partition of community property, it makes sense to permit the creditor to go after only that property that belongs to the debtor. If the spouses have made an equal division of the property, that should be sufficient. If the spouses have made an unequal division to the detriment of the creditor, it is a fraudulent conveyance for which remedies are available.

This is also a result one can reach by taking the view that liability of property for debts should follow management and control. Once the property has been divided, the creditor should reach only property under the debtor's management and control.

The arguments against such a scheme that occur to the staff are that a creditor's vested right to reach community property is affected, that credit will be more difficult for married persons to obtain, and that an interspousal reimbursement action would still be necessary if the debtor spouse is not the person to whom payment was assigned on divorce. These objections do not appear serious to the staff. The creditor's right to reach community property is not really vested since the property can be disposed of by the spouses during marriage to the creditor's detriment; and, in any case, the rule that a creditor can reach only the property of the debtor can be made prospective, thereby divesting only future creditors. The argument that credit will be more difficult to obtain the staff believes is false; the availability of former community property after separation or divorce is not one the factors ordinarily looked to in the extension of credit. An interspousal reimbursement suit against the person who was assigned the debt will be relatively rare since ordinarily the debtor is assigned the debt; in cases where the person who was assigned the debt fails to pay

and the creditor goes after property of the other spouse, a reimbursement suit appears appropriate.

The staff has drafted Section 5120.050 to implement its suggestions. Professor Reppy disagrees with the staff suggestions. He believes that by limiting the property the creditor can reach, the law would encourage claims that the debtor spouse is acting as an agent for the nondebtor spouse in an effort to broaden the liability base. Similarly, persons extending credit would require signatures of both spouses, thereby limiting the ability of one spouse alone to obtain credit.

> Section 5120.050. I am afraid this proposal is going to invite considerable litigation over issues of agency. On its face it seems to make creditors' rights turn on which spouse signs the contract, commits the tort, orders goods, etc. Yet if the acting spouse is in fact operating as an agent for a type of joint venture (e.g., both H and W work at the business for which H signs a contract), agency law will make the other spouse's property liable, too. At present the liability of all community property has practically eliminated to a considerable degree the attractiveness of the agency claim. Section 5120.050 would create a new situation where the claim will be made not only where H and W work in the same business but in the nonbusiness context. For example, if H and W are driving to a social function and W, who usually drives, says she has a headache and asks H to drive, and he commits a tort, why at divorce should community property awarded to W be exempt from liability? The social function was a joint venture for H and W and it was a fortuity H was driving.
>
> The proposed statute will put pressure on credit vendors to get the signature of both spouses so after divorce both are liable. This is contrary to the purpose of the federal equal credit legislation (which compels a credit vendor to grant W alone credit if she has management power over enough property to pay the vendor unless there is some state law that makes the signature of H necessary to protect the creditor vendor — a reason which I think your proposed section 5120.050 creates).

§ 5120.060. Liability of property after judgment of nullity

Professor Reppy points out that the law relating to creditors' rights against property of former "spouses" whose "marriage" has been annulled as void or voidable is not clear. He recommends that the rights of creditors not be affected by the fact that the marriage was invalid. The parties held themselves out as being married and third persons may have relied to their detriment. Professor Reppy believes that fundamental community property principles demand that there be a

community of property formed between the parties even though the marriage is ultimately held invalid. The staff has drafted Section 5120.060 in an attempt to implement Professor Reppy's suggestions.

Marvin Relationships

Professor Reppy recommends enactment of legislation defining creditors' rights in property acquired by parties in a "Marvin" relationship--individuals cohabiting and sharing property pursuant to an express or implied contract. The staff does not believe this would be a profitable undertaking. Such a relationship is difficult to define; the Legislature is currently working, without success, at trying to define it.

Until such a time as there is further useful development in the law, the staff recommends that we do not attempt to prescribe rules. Thus, individuals living together would be treated as individuals for purposes of creditors' remedies, and a creditor would be able to reach only the property of the debtor or the debtor's interest in jointly-held property. Presumably, if there is in fact an express or implied contract, a creditor of one of the parties would be able to reach that party's contract right to the same extent as any other contract right.

Bankruptcy

Section 541(a)(2) of the new Bankruptcy Code provides that the debtor's estate for purposes of bankruptcy includes:

> All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is--
> (A) under the sole, equal, or joint management and control of the debtor; or
> (B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

By specifically including these types of community property in the debtor's estate, is the Bankruptcy Code attempting to preclude a state from providing that some community property is not liable for certain of the debtor's debts?

Under prior law, community property was liable in bankruptcy for the debtor's debts only to the extent provided by state law. See, e.g., In re Wallace, 22 F.2d 171 (E.D. Wash. 1927); cf. Hannah v. Swift, 61

F.2d 307 (9th Cir. 1932) (because community property liable for debts of spouse under state law, it is liable in bankruptcy). Will the bankruptcy courts under the new law ignore the state liability provisions? There are no cases under the new law, but Professor Reppy refers to a law review article finding legislative history to the effect that state nonliability provisions for community property will be ignored. See Comment, The Implications of the New Community Property Laws for Creditors' Remedies and Bankruptcy, 63 Calif. L. Rev. 1610, 1675 (1975).

The staff does not believe this is a real problem. The legislative history mentioned in the law review article relates to an earlier version of the bankruptcy reform effort and not to the Bankruptcy Code provisions as enacted. The staff can find no indication that the law will be any different under the new Bankruptcy Code than under the old Bankruptcy Act. The new Bankruptcy Code makes community property liable for "community claims" against the debtor. 11 U.S.C. § 726(c). A "community claim" is a claim against the debtor for which community property is liable. 11 U.S.C. § 101(b). This appears to incorporate state law governing liability of community property, although there is some indication in the legislative history (House and Senate Judiciary Committee Reports) that a "community claim" is one for which the community property would be liable on a debt of either the debtor or nondebtor spouse. It is noteworthy that the author of the law review article cited above no longer asserts that the new Bankruptcy Code supersedes state community property liability rules. See Pedlar, Community Property and the Bankruptcy Reform Act of 1978, 11 St. Mary's L.J. 349 (1979). The staff believes the bankruptcy courts will respect any provisions of California law governing the liability of community property for the debts of the debtor.

Regardless what the bankruptcy rule is, is there any problem with drafting the California nonliability provisions as "exemptions" rather than as "liabilities"? The staff sees no problem phrasing the provisions as exemptions--it will help insure that the nonliability provisions are recognized in bankruptcy and it will automatically invoke the California exemption procedure in the case of a levy in the state courts. The metaphysical distinction between "not liable" and "exempt" is irrelevant in practice.

Respectfully submitted,

Nathaniel Sterling
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EXHIBIT 1

CHAPTER 3. LIABILITY OF MARITAL PROPERTY

Article 1. General Rules of Liability

§ 5120.010. Liability of community property

5120.010. (a) Except as otherwise expressly provided by statute, the property of the community is liable for a debt of either spouse, whether based on contract, tort, or otherwise, incurred before or after marriage, regardless which spouse has the management and control of the property.

(b) The earnings of a spouse after marriage are exempt from liability for a debt of the other spouse, whether based on contract, tort, or otherwise, incurred before marriage. The earnings remain exempt if they are held in a deposit account by or in the name of the spouse, to the extent they can be traced in the manner prescribed by statute for tracing funds exempt from enforcement of a money judgment. As used in this subdivision, "deposit account" has the meaning prescribed in Section _____ of the Code of Civil Procedure, and "earnings" means compensation for personal services performed, whether as an employee or otherwise.

Comment. Subdivision (a) of Section 5120.010 continues the substance of former Section 5116 (contracts during marriage) and the implication of former Section 5122(b) (torts), and makes clear that the community property (other than earnings of the nondebtor spouse) is liable for the prenuptial contracts of the spouses. Subdivision (a) applies regardless whether the debt was incurred prior to, on, or after January 1, 1975.

The introductory and concluding clauses of subdivision (a) are intended to negate the implication of language found in 1974 Cal. Stats. ch. 1206, § 1, p. 2609, that community property is liable only for the debts of the spouse having management and control. The introductory and concluding clauses make clear that the community property is liable for all debts of either spouse absent an express statutory exemption. Thus community property under the management and control of one spouse pursuant to Section 5125(d) (spouse operating or managing business) or Financial Code Section 851 (one spouse bank account) remains liable for the debts of the other spouse. For an express statutory exemption from liability of community property, see subdivision (b). For an exemption

from liability of former community property after division, see Section 5120.070.

The first sentence of subdivision (b) continues the substance of a portion of former Section 5120 and extends it to include all debts, not just those based on contract. The second sentence codifies the rule that, for purposes of the exemption, earnings may not be traced through changes in form. See, e.g., Pfunder v. Goodwin, 83 Cal. App. 551, 257 P. 119 (1927). Earnings may be traced only into deposit accounts in the same manner as other funds exempt from enforcement of judgments. See Code Civ. Proc. § 703.030 (tracing).

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Tentatively Approved - February 1980

§ 5120.020. Liability of separate property

5120.020. (a) The separate property of a spouse is liable for a debt of the spouse, whether based on contract, tort, or otherwise, incurred before or after marriage.

(b) Except as otherwise expressly provided by statute, the separate property of a spouse is exempt from liability for a debt of the other spouse, whether based on contract, tort, or otherwise, incurred before or after marriage.

Comment. Subdivision (a) of Section 5120.020 continues the substance of a portion of former Section 5121 (contracts) and the implication of former Section 5122(b) (torts); it supersedes former Section 5123 (liability of separate property for debt secured by community property).

Subdivision (b) continues the substance of former Section 5120 (prenuptial contracts), a portion of former Section 5121 (contracts after marriage), and the implication of former Section 5122(b) (torts). For an exception to the rule of subdivision (b), see Section 5120.030 (necessaries of life).

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§ 5120.030. Liability for necessaries

5120.030. (a) Subject to subdivision (b), the separate property of a spouse is liable for a debt of the other spouse incurred after marriage if:

(1) The debt was incurred for necessaries of life of the other spouse while the spouses were living together.

(2) The debt was incurred for common necessaries of life of the other spouse while the spouses were living separate and apart, unless the spouses were living separate and apart by an agreement that waived the obligation of support.

(b) The separate property of a spouse is not subject to enforcement of a money judgment for the debts of the other spouse pursuant to subdivision (a) unless the spouse is a judgment debtor under the judgment.

Comment. Subdivision (a)(1) of Section 5120.030 continues the substance of a portion of former Section 5121, but eliminates the implication that the necessaries must have been contracted for by either spouse. See, e.g., Credit Bureau of San Diego v. Johnson, 61 Cal. App.2d Supp. 834, 142 P.2d 963 (1943) (medical care not contracted by either spouse). Subdivision (a)(1) is consistent with Section 5132 (support obligation while spouses live together) but does not require exhaustion of community and quasi-community property before separate property of a nondebtor spouse can be reached.

Subdivision (a)(2) is consistent with the rule of Section 5131, which preserves the obligation of support between spouses living separate and apart by agreement, unless support is waived in the agreement. Subdivision (a)(2) also abolishes the "station in life" test of cases such as Wisnom v. McCarthy, 48 Cal. App. 697, 192 P. 337 (1920) (maid necessary because of economic and social position of spouses), in determining what is a necessary of life; the separate property of the nondebtor spouse is liable only for debts for the "common" necessaries of life of the other spouse while living separate and apart. Cf. Code Civ. Proc. § 723.051 (common necessaries exception to wage exemption).

Subdivision (b) codifies the rule that the separate property of a spouse may not be subjected to process by necessaries creditors of the other spouse unless the spouse has been made a party and is personally liable on the judgment. See, e.g., Evans v. Noonan, 20 Cal. App. 288, 128 P. 794 (1912); Santa Monica Bay Dist. v. Terranova, 15 Cal. App.3d 854, 93 Cal. Rptr. 538 (1971).

968/667

§ 5120.040. Liability of property after interspousal transfer

5120.040. (a) A transfer of community or separate property between the spouses is subject to the Uniform Fraudulent Conveyance Act, Title 2 (commencing with Section 3439) of Part 2 of Division 4 of the Civil Code.

(b) A transfer of community or separate property between the spouses does not affect the character or ownership of the property for

purposes of the liability of the property for a debt of either spouse incurred before or after the transfer unless both of the following conditions are satisfied:

(1) The transfer is by a written instrument executed and acknowledged or proved by both spouses in the same manner as a grant of real property.

(2) The transfer is recorded in the office of the recorder of the county in which any real property affected by the transfer is located and of the county in which the spouses reside if any other property is affected by the transfer.

Comment. Subdivision (a) of Section 5120.040 codifies existing law. Cf. Bailey v. Leeper, 142 Cal. App.2d 460, 298 P.2d 684 (1956) (transfer of property from husband to wife); Frankel v. Boyd, 106 Cal. 608, 614, 39 P. 939, 941 (1895) (dictum); Wikes v. Smith, 465 F.2d 1142 (1972) (bankruptcy).

Subdivision (b) is comparable to Sections 5114-5115 (inventory of separate property) and Sections 5134-5136 (marriage settlement contracts). For presumptions as to the community or separate character of property, title to which is taken in joint tenancy, see Section _____.

968/697

§ 5120.050. Liability of property after division

5120.050. (a) After division of community and quasi-community property pursuant to Section 4800:

(1) The property owned by a spouse and the property received by the spouse in the division is liable for a debt of the spouse incurred before or after marriage, whether or not the debt was assigned for payment by the other spouse in the division.

(2) Except as otherwise provided in paragraph (3), the property owned by a spouse and the property received by the spouse in the division is exempt from liability for the debts of the other spouse incurred before or after marriage, whether or not assigned for payment by the spouse in the division of the property.

(3) The property owned by a spouse and the property received by the spouse in the division is liable for the debts of the other spouse to

the same extent as provided in Section 5120.030 for the separate property of a spouse.

(b) If the property owned by a spouse or the property received by the spouse in a division of community and quasi-community property pursuant to Section 4800 is applied to the satisfaction of a money judgment for a debt of the spouse that is assigned for payment by the other spouse in the division, the spouse has a right of reimbursement from the other spouse for the market value of the property, with interest at the legal rate, and may recover reasonable attorney's fees incurred in enforcing the right of reimbursement.

Comment. Section 5120.050 prescribes rules of liability of community and quasi-community property and separate or formerly separate property following a division of the property pursuant to a court judgment of separation, dissolution, or later division.

Subdivision (a)(1) states the rule that the rights of a creditor against the property of a debtor are not affected by assignment of the debt to the other spouse for payment pursuant to a property division. A creditor who is not paid may seek to satisfy the debt out of property of the debtor. Former law on this point was not clear. The debtor in such a case will have a right of reimbursement against the former spouse pursuant to subdivision (b).

Subdivision (a)(2) reverses the case law rule that a creditor may seek enforcement of a money judgment against the property of a nondebtor spouse after dissolution of the marriage. See, e.g., Bank of America N.T. & S.A. v. Mantz, 4 Cal.2d 322, 49 P.2d 279 (1935). The community property is liable for the debts of either spouse only during marriage. After a property division under the Family Law Act, however, the creditor must look to the property of the debtor, including former community property assigned to the debtor in the division. If the property division called for the nondebtor spouse to pay the debt and the nondebtor spouse fails to pay, the debtor spouse will have a right of reimbursement pursuant to subdivision (b).

Subdivision (a)(3) is an exception to the rule of subdivision (a)(2). It preserves the liability of the nondebtor spouse for necessaries of the debtor spouse. Under Section 5120.030, such liability does not exist if the debt was incurred while the spouses were living separate and apart.

Subdivision (b) states the rule as to reimbursement where a debt is satisfied out of the property of a spouse other than the spouse to whom the debt was assigned pursuant to a property division. Former law on this point was not clear.

§ 5120.060. Liability of property after judgment of nullity

5120.060. After a judgment of nullity of a marriage, whether void or voidable, the property that would have been community property and the property that would have been the separate property of the parties had the marriage been valid is liable for the debts of the parties to the same extent as if the marriage were valid and the judgment of nullity were a judgment of dissolution, regardless whether the parties are declared to have the status of putative spouses and regardless whether the property is quasi-marital property.

Comment. Section 5120.060 is consistent with Section 4451 (judgment of nullity conclusive only as to parties to the proceeding). Former law was not clear.

EXHIBIT 2

CONFORMING CHANGES

Civil Code § 5116 (repealed)

~~5116. The property of the community is liable for the contracts of either spouse which are made after marriage and prior to or on or after January 1, 1975.~~

Comment. The substance of former Section 5116 is continued in Section 5120.010(a).

992/943 N/Z

Civil Code § 5120 (repealed)

~~5120. Neither the separate property of a spouse nor the earnings of the spouse after marriage is liable for the debts of the other spouse contracted before the marriage.~~

Comment. The portion of former Section 5120 exempting separate property of a spouse from liability for the debts of the other spouse contracted before marriage is continued in Section 5120.020(b). The portion exempting earnings after marriage is continued in Section 5120.010(b).

17022 N/Z

Civil Code § 5121 (repealed)

~~5121. The separate property of a spouse is liable for the debts of the spouse contracted before or after the marriage of the spouse, but is not liable for the debts of the other spouse contracted after marriage; provided, that the separate property of the spouse is liable for the payment of debts contracted by either spouse for the necessaries of life pursuant to Section 5132.~~

Comment. The substance of former Section 5121 is continued in Section 5120.020.

Civil Code § 5123 (repealed)

~~5123. (a) The separate property of the wife is not liable for any debt or obligation secured by a mortgage, deed of trust or other hypothecation of the community property which is executed prior to January 1, 1975, unless the wife expressly assents in writing to the liability of her separate property for such debt or obligation.~~

~~(b) The separate property of a spouse is not liable for any debt or obligation secured by a mortgage, deed of trust, or other hypothecation of the community property which is executed on or after January 1, 1975, unless the spouse expressly assents in writing to the liability of the separate property for the debt or obligation.~~

Comment. Section 5123 is not continued and is superseded by Section 5120.020. It is a form of antideficiency judgment that protects some but not all assets of a spouse for obligations secured by any community property, real or personal, residential or otherwise. It is thus inconsistent with general rules governing deficiency judgments.

968/710

Civil Code § 5131 (amended)

5131. A spouse is not liable for the support of the other spouse when the other spouse is living separate from the spouse by agreement ~~unless~~ that waives such support ~~is stipulated in the agreement~~ .

Comment. Section 5131 is amended consistent with Section 5120.030(a)(2), which continues the liability of property of spouses for necessaries after separation unless expressly waived in the separation agreement.

15797

Civil Code § 5132 (amended)

5132. Subject to Section 5120.030:

(a) A spouse must support the other spouse while they are living together out of the separate property of the spouse when there is no community property or quasi-community property.

(b) For the purposes of this section, the terms "quasi-community property" and "separate property" have the meanings given those terms by Sections 4803 and 4804.

Comment. Section 5132 is amended to make clear that it does not apply to situations covered by Section 5120.030 (liability for necessaries). The two provisions are consistent but Section 5120.030(a)(1) does not require exhaustion of community and quasi-community property before separate property of a nondebtor spouse can be reached by a third-party creditor.

045/077

Civil Code § 5135 (amended)

5135. When such contract is acknowledged or proved, it must be recorded in the office of the recorder of every county in which real estate may be situated which is granted or affected by such contract and in the office of the recorder of the county in which each spouse resides if personal property is granted or affected by the contract .

Comment. Section 5135 is amended to require recordation of a marriage settlement contract in the county where the spouses reside if the contract affects personal property. This requirement will result in constructive notice to third parties such as creditors. For comparable provisions, see Sections 5114 (recordation of list of separate personal property) and 5120.040(b) (liability of property after interspousal transfer).

EXHIBIT 3

TO: Nat Sterling

FR: Marcia Grimm

DA: 20 March, 1980

RE: Transmutation of Community Property in States Other Than California

1. ARIZONA

A. Extent of Transmutation

In Arizona, all property acquired by either husband or wife during marriage is community property except that acquired by gift, devise, or consent. Ariz. Rev. Stat. Ann. § 25-211. Community property may be conveyed from one spouse to the other, vesting title in the latter as separate property, provided only that the donating spouse intends to make a gift to the other. See, e.g., Germania Fire Ins. Co. v. Bally, 19 Az. 580, 173 P. 1052 (1918); Schofield v. Gold, 26 Az. 296, 225 P. 71 (1924). In Blaine v. Blaine, 63 Az. 100, 159 P.2d 786 (1947), the court found that a husband who purchased property with his separate funds and took the deed in his wife's name as well as his own had made a gift to his wife of one-half interest in the property, thus transforming it into community property. A quitclaim deed of a wife in favor of her husband transforms her separate property into community property, if the surrounding facts indicate this was her intention and the deed fails to specify that it is the husband's separate property. Arizona Central Credit Union v. Holden, 6 Az. App. 310, 432 P.2d 276 (____). Property purchased with community funds also becomes the individual property of the title holder, if the other spouse consents and has the intention of making a gift. Jones v. Rigdon, 32 Az. 286, 257 P. 639 (1927); Germania Fire Ins. Co. v. Bally, 19 Az. 580, 173 P. 1052 (1918).

Under Az. Rev. Stat. Ann. § 25-201, parties may make antenuptial agreements "not contrary to good morals or law." A matrimonial agreement must be acknowledged before an officer authorized to acknowledge deeds. (See Spector v. Spector, 23 Az. App. 131, 531 P.2d 176 (1975).) There is no statutory prohibitian of spousal contracts affecting property interests made after marriage. See Lay, Transmutation of Community Property, 18 S. Carolina L. Rev. 755, 759-80 (1966). (NB: The statute pertaining to antenuptial

contracts was amended in 1973 to delete a sentence forbidding the parties to alter the law of descent.)

B. Formalities Required.

A gift of real property from one spouse to the other is evidenced by a conveyance and proof of intention. Jones v. Rigdon; Lincoln Fire Insurance v. Barnes, 53 Az. 264, 88 P.2d 533 (1939); In re Sims' Estate, 13 Az. App. 228, 475 P.2d 505 (1970). In some cases a transmutation of property may be found in the absence of an explicit agreement, if circumstances clearly show that one spouse intended to alter the status of his property. This is true of personal property (Lightening Delivery Co. v. Matteson, 45 Az. 92, 39 P.2d 938 (1935)) and separate property litigated as community (Moser v. Moser, 117 Az. 312, 572 P.2d 446 (1977) (insurance policies)). In Schock v. Schock, 11 Az. App. 53, 461 P.2d 697 (1969), the court considered the fact that other jurisdictions have found transmutations effected by oral agreement, but thought the evidence insufficient for such a finding in that case, since the court found the husband's statements actually negated a transmutation claim. 461 P.2d 701.

C. Rights of Creditors

Spouses may not convey or sever their property to the detriment of creditors. Lincoln Fire Ins. Co. v. Barnes; Jones v. Rigdon. Where separate property subject to a loan is transmuted into community property, it remains subject to the debt and the value of the community interest is its fair market value less the amount of the debt unless the parties agree otherwise at the time of the transaction. Moser v. Moser, 572 P.2d at 449.

2. IDAHO

Any conveyance from one spouse to the other is presumed to be a gift to the grantee's separate estate, when the deed or other instrument of title is acknowledged by the grantor. Idaho Code Ann. § 32-906. The use of community funds to improve the wife's separate property is presumed a gift from the husband, Bank of Orofino v. Wellman, 26 Idaho 425, 143 P. 1169 (1914). Property

owned before marriage or acquired afterward by gift, bequest, devise or descent, or with the proceeds of separate property, is to remain separate property under Section 3-903.

Idaho also permits any two persons to open a joint bank account with a right of survivorship. Idaho Code Ann. § 26-1014. When there is evidence the survivorship right was intended by the parties, this procedure may effect a transfer of community property into joint tenancy. See Transmutation of Community Property, 18 S. Carolina L. Rev. at 764.

A gift made while the donor owes outstanding debts is void as to existing creditors, Hobbs v. Hobbs, 69 Idaho 201, 204 P.2d 1034 (1949); Glover v. Brown, 32 Idaho 426, 184 P. 649 (1919). However, if the donor has other property to satisfy creditors' claims, the gift will not be set aside as a fraudulent conveyance. McMillan v. McMillan, 42 Idaho 270, 245 P. 98 (1926).

3. LOUISIANA

A. Transmutation

Title VI of Book III (Arts. 2325-2376) of Louisiana's Civil Code was revised in 1978 to create a new matrimonial regimes law (Acts 1979, No. 709). Article 2328 provides:

> A matrimonial agreement is a contract establishing a regime of separation of property or modifying or terminating the legal regime. Spouses are free to establish by matrimonial agreement a regime of separation of property or modify the legal regime as provided by law. The provisions of the legal regime that have not been excluded or modified by agreement retain their force and effect.

Such agreements may be made before or during marriage as to all matters not prohibited by public policy, and may be modified or terminated during marriage upon a joint petition and finding by the court that this serves the best interests of the parties and that they understand the governing principles and rules. LSA Civ. Code, art. 2329. Article 2330 provides that spouses may not, by agreement before or during marriage, alter or renounce the marital portion or the established order of succession.

Spouses may also make gifts to each other (LSA Civ. Code, Art. 1746) except that they cannot make "any mutual or reciprocal dona-

tion by one and the same act" (LSA Civ. Code art. 1751). A donation of one spouse's undivided interest in part of the community to the other transforms that interest, and also the equal interest of the donee spouse into the donee's separate property. LSA Civ. Code, art. 2343.

B. Formalities

A marital contract must be made by authentic act or by an act or by an act under private signature duly acknowledged by the parties. LSA Civ. Code, art. 2331. Under Article 2234 of the same code, an authentic act is defined as one executed before a notary public or other authorized officer with two witnesses, and also includes all "proces verbal of sales of succession property," signed by the sheriff and two witnesses. A modification or termination of a contractual marital regime during the marriage requires court approval. LSA Civ. Code, art. 2329.

Louisiana Civil Code, Article 2332, provides that a marital agreement or a judgment establishing a regime of separation of property is effective toward third parties only when filed for registry; in the case of immovable property, in the conveyance records of the parish in which the property is situated, and as to movables, in the parish(es) where the spouses are domiciled.

In Succession of Broussard, 306 So.2d 399, 402 (App. 1975), the court stated that a manual gift of corporeal effects accompanied by real delivery is not subject to any formality. However, the court held that the wife's (incorporeal) business earnings and profits were community property because she failed to support her testimony with evidence of her husband's donative intent. In the absence of proof of a manual gift, donations have been held invalid for failure to pass before a notary and two witnesses. Succession of Coste, 43 La. Ann. 144, 9 So. 92 (1891); Atkinson v. Atkinson, 15 La. Ann. 491 (1860).

C. Rights of Creditors

A marital agreement or donation from one spouse to the other in fraud of creditors may be set aside by revocatory actions under Articles 1969-1994 of the Civil Code. See Civil Code, Arts. 2328, 2329 and 2343, and Comments thereto. Similarly, Civil Code,

Article 1502 provides that any disposal of property exceeding the quantum legally disposable to the prejudice of forced heirs is reducible to that quantum. See Comments to LSA Civ. Code, Art. 2328.

4. NEW MEXICO

In 1973, New Mexico also altered its community property law, if in somewhat more comprehensible fashion than Louisiana. NMSA Section 40-3-2 now provides that a husband and wife may hold property as joint tenants, tenants in common, or in community. Separate property includes property (1) acquired before marriage or after a decree of dissolution; (2) designated as separate property by court decree; (3) acquired by either spouse by gift, bequest, devise or descent; (4) designated as separate property by a written agreement between the spouses; and (5) constituting each spouse's undivided interest in property owned by the spouses as joint tenants or tenants in common. NMSA § 40-3-8.

Property acquired during marriage is generally presumed to be community property, except that where a written instrument in the married woman's name alone (or in her name and that of someone else not her husband) was delivered and accepted prior to July 1, 1973, the property so acquired is presumed separate. Section 40-3-12.

Thus a transmutation of property between the spouses should be by written agreement. Gifts not accompanied by a written instrument must be supported by "clear, strong and convincing proof--more than a mere preponderance of evidence." In re Trimble's Estate, 57 NM 51, 57, 253 P.2d 805, 808 (1953).

A deed transferring real estate to a spouse's separate property may be attacked by creditors for fraud. In the absence of actual fraud, and unless made as a cover for further fraud, it may not be attacked by creditors whose debts arose after the transfer. If attacked by a preexisting creditor and set aside, however, all creditors, prior and subsequent, are entitled to a pro rata share of the funds from sale of the property. Ilfield v. DeBaca, 13 NM 32, 79 P. 723 (1905).

5. NEVADA

A. Transmutation

Nevada law provides that a husband and wife may enter into contracts with one another (Nev. Rev. Stats. § 123.070), and may thereby alter their legal relations in property by mutual consent (NRS § 123.080).

A transmutation of community property into separate property of either spouse may be effected by (1) an agreement in writing between the spouses, which is effective only as between them (NRS § 123.220(1)); (2) a decree of separate maintenance issued by a court (NRS § 123.220(2)); (3) written authorization of one spouse, permitting the other to appropriate his/her own earnings to his/her own use (NRS §§ 123.090, 123.220(3)). By definition, any property acquired by gift, bequest, descent or devise is separate property (NRS § 123.130) and spouses may make gifts to one another. Petition of Fuller, 63 Nev. 26, 159 P.2d 579 (1949); Stockgrowers & Ranchers Bank v. Milisich, 52 Nev. 178, 283 P. 913 (1930). Where the husband expends separate or community funds for improvements to the wife's separate property, a gift to the wife is presumed, in the absence of agreement to the contrary. Lombardi v. Lombardi, 44 Nev. 314, 195 P. 93 (1921).

The spouses may also hold property as joint tenants or tenants in common (NRS § 123.030). Joint tenancy property can be contractually converted to community property, upon sufficient proof of agreement and intent. See Milliken v. Jones, 7 Nev. 15, 278 P.2d 876 (1955).

B. Formalities

Under the statutes, an agreement to convert community property to separate property must be in writing. NRS §§ 123.080, 123.090. A transfer of property by deed creates only a presumption that transmutation was intended, however, which may be rebutted by evidence to the contrary. Pehhon of Fuller, 63 Nev. 26, 159 P.2d 579 (1945).

A transmutation by gift may be inferred from the conduct of the parties and from subsequent transactions of the donee (Stockgrowers & Ranchers, 283 P. at 915), although the "mere naked

statement of gift" will not suffice (Milisich v. Hillhouse, 48 Nev. 166, 228 P. 307 (1924)).

C. Rights of Creditors

A transmutation agreement is, by statute, only effective as between the spouses (NRS § 123.220(1)). In a suit to subject notes held by a wife to payment of a judgment against her husband, the court held that "a motive to place his property beyond the reach of creditors cannot be charged against the bona fides of the gift transaction," where the husband owed no debts at the time of the gift. Stockgrowers & Ranchers, 283 P. at 914. "The facility with which fraud may be consummated under pretense of gifts between husband and wife is merely to be kept in mind in weighing the evidence bearing on such an issue." Id.

6. TEXAS

Article 16, Section 15 of the Texas Constitution provides:

> All property, both real and personal, of the wife, owned or claimed by her before marriage, and that afterward acquired by gift, devise, or descent, shall be the separate property of the wife; . . . husband and wife, without prejudice to pre-existing creditors, may from time to time as if the wife were a feme sole partition between themselves in severalty or into equal undivided interests all or any part of their existing community property, or exchange between themselves the community interest of one spouse in any property for the community interest of the other spouse in other community property, whereupn the portion or interest set aside to each spouse shall be and constitute a part of the separate property of such spouse.

The constitutional provision is implemented in Texas Family Code, Title I, Section 5.42 (1970), providing that a partition or exchange as authorized by the Constitution must be in writing and subscribed by both parties (Section 5.42(a)). Property or property interests transferred to a spouse under partition or exchange becomes the separate property of that spouse, subject to two conditions: The partition or exchange cannot prejudice the rights of preexisting creditors (Section 5.42(c)), and, as to real property, the agreement is not constructive notice to a good faith purchaser for value or a creditor without actual notice unless the instrument is acknowledged and recorded in the county in which the real prop-

erty is located (Section 5.42(d)). Any derivations from the statutory procedures will render a severance invalid (Reed v. Reed, 283 SW2d 311 (Tex. Civ. App. 1955); Hilley v. Hilley, 161 Tex. 569, 342 SW2d 565 (1961), and void against creditors (Amarillo Nat'l Bank v. Liston, 464 SW2d 395 (1970)).

In order to transfer community property into joint tenancy a two-step procedure must be followed. First, partition of the community property must be effected in accordance with the provisions of the statute; then, and only then, a joint tenancy agreement with the right of survivorship may be entered into. Bowman v. Simpson, 546 SW2d (Civ. App. 1976). A statute providing that husband and wife may enter into a savings contract constituting a partition of community property and creating a joint tenancy with a right of survivorship (Tex. Probate Code art. 852a, § 6.13) was held unconstitutional in Williams v. McKnight, 402 SW2d 505 (1966), on grounds that the statutory procedures for partition in Family Code Section 5.42 (then Civ. Stat. art. 4624a) must be followed. The only possible exception is in the case of U.S. Treasury Bonds, where the interests of the federal government as borrower are concerned and federal regulations provide that a surviving co-owner becomes the absolute and sole owner upon death of the other co-owner. Free v. Bland, 396 U.S. 663 (1962); Bowman v. Simpson, 546 SW2d at 101.

A spouse may make a gift of his/her separate property or interest in the community property, to the other spouse, and this will convert it to the donee's separate property, so long as this does not interfere with the rights of creditors. Schroff v. Dedton, 220 SW2d 489 (Tex. Civ. App. 1949); Cauble v. Bearer-Electra Refining Co., 115 Tex. 1, 274 SW 120 (1925). However, a gift to the community may not be made from the separate property of either spouse. Kellett v. Trice, 95 Tex. 160, 66 SW 51 (1902); Tittle v. Tittle, 148 Tex. 102, 220 SW2d 637, 643 (1949); Higgins v. Higgins, 458 SW2d 498 (1970).

7. WASHINGTON

A spouse may give, grant, sell or convey directly to the other spouse, all or part of his/her interest in the community real

property, thereby divesting the property so transferred of all claims and demands as community property and vesting it in the donee spouse as separate property. Wash. Rev. Code 26.16.050. The statute requires the grantor to sign, seal and acknowledge the deed as a single person, without joinder of the person named as grantee (id.), and oral agreements are not sufficient (Rogers v. Jouqlin, 152 Wn. 448, 227 P. 988 (1929)). Such transfers shall not effect any existing equity in favor of the transfer, gift or conveyance (Wash. Rev. Code § 26.16.050) and thus are void against existing creditors (Sallske v. Fletcher, 73 Wash. 593, 132 P. 648 (1913).

Where a husband purchases property in his wife's name with separate funds, a gift is presumed, and the burden is one attacking the validity of the gift to overcome the presumption. Scott v. Cline, 7 Wash.2d 301, 109 P.2d 526 (1941).

Transfers of personal property are not covered by the statute but the courts have upheld oral agreements between the spouses that each shall retain their separate earnings. Union Securities Co. v. Smith, 93 Wash. 115, 160 P. 304 (1916); In re Jansen's Estate, 56 Wash.2d 150, 351 P.2d 510 (1960). A gift of personal property must be supported by evidence of clear, certain and convincing character. In re Slocum's Estate, 83 Wash. 158, 145 P. 204 (1915) (mere fact of possession insufficient evidence of gift of stock certificates). Moreover, a severance agreement may be defeated by evidence of its nonobservance. Kolmorgan v. Schaller, 316 P. 111.

A husband and wife may also jointly enter into any agreement concerning the status or disposition of community property to take effect upon the death of either. WRC 26.16.120. The statute requires that such an agreement by made "by the execution of an instrument in writing under their hands and seals, and . . . witnessed, acknowledged and certified in the same manner as deeds to real estate are required to be," and shall not derogate from the rights of creditors. Id.

EXHIBIT 4

Duke University
DURHAM
NORTH CAROLINA

SCHOOL OF LAW POSTAL CODE 27706

February 12, 1980

Mr. Nat Sterling
California Law Revision Commission
Stanford Law School
Stanford, California 94305

Dear Nat:

A further thought after I mailed you yesterday some comments on the staff proposal for a statute requiring recordation of transmutation agreements if they are to bind creditors of a spouse: as I read the present Civil Code section 5135, an antenuptial contract that alters the normal rules of classification of property (e.g., the most common form thereof, that acquisitions of both H and W will be separate property) need not be recorded to bind creditors insofar as personal property is concerned. (The statute requires recordation, obviously to benefit third parties, only in the county where affected land is situated.) I think section 5135 should either be repealed or amended to indicate that recordation is also necessary to bind third party creditors where personal property is at issue and is transmuted under an antenuptial contract.

Sincerely,

William A. Reppy, Jr.
Professor of Law

WAR:jma